The Creation of an Expense Account Society

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Abstract

Almost immediately after lockdowns were announced in response to the COVID-19 pandemic, President Donald Trump called for restoring the deduction for business meal and entertainment expenses that had been removed in 2017. Perhaps imagining that it would result in a return to the post-World War II era when lavish spending was common, Trump hoped it would rescue a sinking restaurant industry. In a sense, he was right to connect tax with business meals and entertainment. Expense accounts, and the industry that evolved to support it, were a creature of the high post-war tax rates that persisted through the 1950s and beyond. Understanding the rise of this phenomenon, and the forces that conspired to defeat President John F. Kennedy proposal to eliminate deductions for meals and entertainment, helps to explain how inextricably linked tax is with business spending on meals and entertainment and how it became entrenched in American society.

In 2017, as part of President Donald Trump's Tax Cuts and Jobs Act, Congress removed the deduction for expenses considered to constitute "entertainment, amusement, or recreation," including most business meals, to help to pay for tax cuts elsewhere in the bill.[1] This removal, however, did not even last the length of Trump's presidency unscathed. Within weeks of the announcement of lockdowns in March 2020, Trump urged Congress to restore the full deduction

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[1] I.R.C. §274(a)(1)(A). It was not entirely clear that the deduction for business meals was actually removed as part of the elimination of the deduction for entertainment expenses. The IRS issued a notice suggesting that business meals were still deductible, see Notice 2018-76, but the Joint Committee on Taxation concluded that business meals were generally considered entertainment expenses, and therefore no longer deductible, unless provided to employees as de minimis fringe benefits or for the convenience of the employer. Joint Committee on Taxation, *Overview of the Federal Tax System as in Effect for 2018* (JCX-3-18) at 13, n. 44 (Feb. 7, 2018).

for meals and entertainment expenses as an aid to the restaurant and hospitality industry.[2] Although few believed that tax deductions were likely to do much, if anything, to save struggling restaurants and hotels during the pandemic,[3] Trump doubled down on his crusade for reviving the so-called "Three Martini Lunch."[4] By early December, Trump finally managed to get a deduction inserted at least for business meals into a COVID relief bill. Under the Taxpayer Certainty and Disaster Relief Tax Act of 2020, all business-related "food or beverages provided by a restaurant" prior to January 1, 2023 are eligible for a full deduction.[5]

The resilience of the deduction for meals and entertainment recalls a similar episode in American tax history. In 1961, amidst growing concern about tax avoidance, President John F. Kennedy proposed to eliminate the tax deduction for travel and entertainment expenses. There were limited exceptions for certain food and beverage expenses, but these were for narrow circumstances such as while away from home on business or while at work or during business meetings.[6] Taking clients out to lunch or dinner merely for the purpose of generating goodwill would have been strictly prohibited.[7] Moreover, even permitted exceptions would have been subject to strict monetary limits, estimated between four and seven dollars per day.[8] The effect of

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[2] TRUMP WANTS CONGRESS TO RESTORE FULL TAX DEDUCTION FOR MEALS, ENTERTAINMENT, REUTERS, March 29, 2020, *available at* https://www.reuters.com/article/us-health-coronavirus-taxes/trump-wants-congress-to-restore-full-tax-deduction-for-meals-entertainment-idUSKBN21G0YB.

[3] Howard Gleckman, *Restoring the Three Martini Lunch Tax Deduction Won't Feed the COVID-19 Economy*, TAX VOX: BUSINESS TAXES, May 7, 2020, available at https://www.taxpolicycenter.org/taxvox/restoring-three-martini-lunch-tax-deduction-wont-feed-covid-19-economy; Darla Mercado, *"Three Martini Lunch" Tax Break May Not Save Many Restaurants, Advisors Say*, CNBC, Dec. 21, 2020, available at https://www.cnbc.com/2020/12/21/three-martini-lunch-tax-break-could-fall-short-for-vulnerable-eateries.html.

[4] For a history of that term, see Joseph Thorndike, *A Cultural History of the Three-Martini Lunch*, FORBES, Jan. 21, 2021, available at https://www.forbes.com/sites/taxnotes/2021/01/21/a-cultural-tax-history-of-the-three-martini-lunch/"sh=1e99d84ee3f0.

[5] Rules Committee Print 116-68, Text of the House Amendment to the Senate Amendment to H.R. 133 of the Consolidated Appropriations Act of 2021, Dec. 21, 2021, § 210 (Amending 274(n)(2)).

[6] Norman H. Lipoff, *Entertainment and Related Expenses Under Legislative Attack*, 17 TAX L. REV. 183, 193-94 (1962).

[7] Id. at 194.

[8] Id.

these limits would have been to eliminate most of the meals normally written off as business expenses.

After intense lobbying from the entertainment, hospitality, and restaurant industries, Congress pulled back from Kennedy's original proposal. Rather than repealing the deductions altogether, Congress permitted them so long as they were "directly related" to the active conduct of a taxpayer's trade or business or they were at least "associated with" the active conduct of the taxpayer's trade or business and the entertainment activities directly preceded or followed a "substantial and bona fide business discussion."[9] The deduction for business meals was treated even more favorably. As ultimately adopted in the Revenue Act of 1962, business meals were specifically exempted from the guardrails imposed on other forms of entertainment to ensure that they were business-related.[10]

Trump's focus on the restaurant industry was arguably not a mere pandemic relief measure. As with his campaign slogan to "Make America Great Again," Trump likely was thinking in part about restoring the same post-War era society that led to Kennedy's proposal.[11] The development of the expense account society at this time laid the foundation for his own subsequent participation in and profit from its practices when he was coming of age in business. Lavish spending on restaurants and entertainment was not only common among the wealthy, but it was common among many regular workers too because of the tax benefits provided to the businesses that subsidized

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[9] Michel G. Emmanuel & Norman H. Lipoff, *Travel and Entertainment: The New World of Section 274*, 18 TAX L. REV. 487, 489 (1963).
[10] Id. at 495.
[11] Kim Chatelain, *If Not Now, When was American Great*? NOLA.COM, July 19, 2019, available at https://www.nola.com/news/politics/article_9aba017c-499c-5a11-98e6-6b5ce6b563b1.html (noting that Trump has cited the late 1940s and nearly 1950s as one era when America was great and that others agree that he "is harkening to the period after World War II when U.S. military muscle bulged and the economy was growing" at a high rate).

the practice. Indeed, expense accounts, and the industry that evolved to support it, were a creature of the sky-high World War II tax rates that lingered long after the end of the war and society's attempt to find a way to maintain their incomes in the face of those rates or to keep up with those of their competitors who were using it in this way. As Treasury Secretary Douglas Dillon testified in 1961, "much of [expense account abuse] is done in response to competitive pressure which has in large measure been created by tax law and not by the dictates of business." [12] It therefore should not have been surprising that Trump immediately turned to the tax laws in his bid to revive that era. Studying Kennedy's proposal and its defeat helps to explain how inextricably linked the rise of the expense account society and its persistence has been with the tax system and popular sentiments about it.

The origins of expense accounts

Spending on meals and entertainment to woo customers and clients has a long history. According to Philip Stern, "The expense-account problem is ancient. During the last half-century of the Roman Republic, traveling Roman senators enjoyed what was known as 'Legatio Liberia,' by which they could charge their traveling expense against the people they visited." Later, the allowable expenses were limited to "beds and bedding, hay and fodder, firewood and sale."[13]

This practice of allowing a deduction for expenses to entertain current and prospective customers in the commercial sector started in the United States when first post-Sixteenth

[12] See Hearings before House Committee on Ways and Means on the Tax Recommendations of the President Contained in his Message Transmitted to Congress, April 20, 1961, 87th. Cong., 1st Sess. 42 (1961) (Statement of Treasury Secretary Dillon) ("Hearings on President Kennedy's Special Message").
[13] Stern, supra note xx, at 111.

Amendment income tax was enacted in 1913. At that time, deductions were allowed for "the necessary expenses actually paid in carrying on any business."[14] Congress was careful even then, however, to make clear that the deduction for business expenses would not extend to "personal, living or family expenses."[15] Congress specifically permitted the deduction of travel expenses for business in the Revenue Act of 1921 and added membership in business and trade organizations and attendance at their meetings in the Revenue Act of 1928.[16] Treasury further reinforced the distinction between business and personal travel when it issued regulations defining deductible travel as solely for business purposes, leaving all other travel as personal,[17] although the "solely" language was generally interpreted so as to permit a deduction as long as the "primary purpose" was business.[18]

Despite the distinction between business expenses – which were deductible – and personal expenses – which were non-deductible – there was little attempt to identify a method to keep track of the former and distinguish them from the latter. Indeed, the long-standing Cohan rule – which permitted taxpayers to deduct expense accounts without any detailed receipts or documentation until the early 1960s – derived from a 1930 case in which a Broadway producer had been "free-handed in entertaining actors, employees, and, as [the producer] naively adds, dramatic critics," in 1921 and 1922.[19] The taxpayer, though, "kept no account" of his expenses and the Board of Tax

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[14] Revenue Act of 1913, Pub. L. No. 63-16, 38 Stat. 167 (1913).
[15] Id.
[16] Revenue Act of 1921, Pub. L. No. 67-98, 42 Stat. 227 (1921); Revenue Act of 1928, Pub. L. No. 70-562, 45 Stat. 791 (1928). During this period, the primary concern was over travel and per diem expenses, rather than entertainment more broadly. Mortimer M. Caplin, *The Travel and Entertainment Expense Problem*, 39 TAXES 947 (1961).
[17] Treas. Reg. 101, §23(a)-2 (1939) ("if the trip is undertaken for other than business purposes, the railroad fares are personal expenses . . . [but] if the trip is solely on business," the fares are deductible.
[18] William A. Klein, *The Deductibility of Transportation Expenses of a Combination Business and Pleasure Trip – a Conceptual Analysis*, 18 STAN. L. REV. 1099, 1105 (1966).
[19] Cohan v. Commissioner of Internal Revenue, 39 F.2d 540, 543 (2d Cir. 1930).

Appeals denied his deductions "on the ground that it was impossible to tell how much he had in fact spent, in the absence of any items or details."[20] The Second Circuit, however, overturned the decision, with Judge Learned Hand writing that "absolute certainty in such matters is usually impossible and is not necessary; the Board should make as close an approximation as it can."[21] Hand acknowledged that "we do not know how many trips Cohan made, nor how large his entertainments were," but concluded that "there was basis for some allowance, and it was wrong to refuse any."[22]

World War II and the rise of the expense account

Notwithstanding the free hand afforded to businessmen to deduct entertainment expenses, it was not until World War II that the expense account truly took off.[23] In large part, "the great expense account charade" began with the enactment of an excess profits tax in World War II.[24] This tax, an add-on to the income tax already applied to corporate income, purported to capture the profits corporations were earning as a windfall from the government's mobilization of the

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[20] Id. at 543.
[21] Id. at 544.
[22] Id.
[23] *See* Richard Gehman, *Expense Accounts*, COSMOPOLITAN, March 1957, at 44-47 in U.S. Treasury Department, Study on Entertainment Expenses in President's Tax Message along with Principal Statement, Detailed Explanation, and Supporting Exhibits and Documents submitted by Secretary of the Treasury Douglas Dillon in connection with the President's Recommendations Contained in his Message on Taxation at Hearings conducted by Committee on Ways and Means, House of Representatives (May 3, 1961), Exhibit V, at 243. ("Study on Entertainment Expenses") ("Ever since World War II, the expense account has been playing an increasingly important part in our lives and our economy.").
[24] Michael G. Emmanuel and Norman H. Lipoff, *Travel and Entertainment: The New World of Section 274*, 18 Tax L. Rev. 487, 487 (1963). *See I'll Just Sign: Those Big-Figure Expense Accounts*, NEWSWEEK, May 20, 1957, at 87 ("Taxes, of course, have been largely responsible for the postwar boom in expense accounts; until 1954, the combined income and excess profits tax of 82 percent on the income of a big corporation meant that each expense account dollar cost the company only 18 cents."); John D. Pomfret, *"Expense Account Living" Coming Under Close Scrutiny*, N.Y. TIMES, Dec. 10, 1962, at 13 ("In the high-tax, relatively free spending years of World War II, the new phenomenon of expense-account living burst on the American business scene.").

economy for wartime production.[25] It levied a penalty upon the profits corporations made beyond a "normal" return, which Congress defined to be, at the election of the taxpayer, either the average of the earnings in the three pre-war years or an amount of earnings on invested capital beyond five percent (or 8 percent for smaller businesses).[26] Although the World War II excess profits tax was repealed in 1945, it was revived in 1950 as the Korean conflict began.[27] By 1952, with the corporate income tax rate at 52 percent and the excess profits tax rate an additional 30 percent,[28] the burden on business was crushing and the temptation to look for additional deductions was overwhelming.

Under these corporate and excess profits tax rates, it was not surprising that the expense account flourished. After all, deductible entertainment expenses only cost companies 18 cents for every dollar spent, making it easy for employees to justify expenses that might otherwise have garnered greater scrutiny.[29] Moreover, these rates came at a time when many companies were flush with cash because of wartime profits. According to one Pennsylvania manufacturer, "expense account spending first reached a peak during World War II when the companies had more money than ever before and couldn't keep it because of taxes."[30] Because of this, "they had to throw it around, and they did it by advertising and entertaining."[31]

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[25] STEVEN A. BANK ET AL, WAR AND TAXES 87-88 (2008).
[26] Id. at 88-89. See Carl Shoup, *The Concept of Excess Profits Under the Revenue Acts of 1940-42*, 10 L. & CONTEMP. PROBS. 28, n. 2 (1943) (explaining that although taxpayers almost evenly divided in choosing between the two methods, the aggregate excess net excess profits income of those using the base-period method was more than double that of taxpayers using the invested capital method).
[27] Id. at 117.
[28] Federal Corporate Income Tax Rates, Income Years 1909-2012, Tax Foundation, July 6, 2012, available at https://taxfoundation.org/federal-corporate-income-tax-rates-income-years-1909-2012/.
[29] Ernest Havemann, *The Expense Account Aristocracy: Tax Deductions 'For Business Purposes' Make it Cheap to Live*, LIFE MAG., March 9, 1953, at 140.
[30] Richard Gehman, *Expense Accounts*, COSMOPOLITAN, March 1957, at 44, 45 (1957).
[31] Id.

Although it was difficult to get a complete picture of expense account spending, it was estimated to be between $5 and $10 billion annually, with the deduction resulting in a $1 to $2 billion loss of revenue.[32] This included not only business lunches, but also entertainment and gifts. A 1960 Internal Revenue Service study of 38,000 federal income tax returns provided a peek at where those expense accounts were being spent. It found that in the small universe of returns, $11 million was spent on business gifts, $5.7 million was spent on dues for private clubs, $2.6 million went toward yachts, $2 million was for theater tickets, and $1 million was for hunting lodges and fishing camps.[33]

Businesses were not shy about citing the high rates specifically as justification for continuing to be generous in allowing expense deductions. As George Newman, a representative of the Iowa Manufacturers Association testified before the House Ways and Means Committee, "viewed in light of the present combined top corporate rate of tax on net profits, of 52 percent, and the steeply graduated of individual tax going up to 91 percent which apply to the net income of unincorporated businesses, erosion of the "ordinary and necessary" rule would be economic folly."[34]

In addition to the lure of deductible expenses, companies were also motivated to provide their employees with tax exempt compensation. The *Wall Street Journal* explained that by 1958 "the expense account has become, willy-nilly, an adjunct to salary."[35] In an era of high individual marginal rates, converting taxable compensation to non-taxable benefits was a way to ease the

[32] JEROME R. HELLERSTEIN, TAXES, LOOPHOLES, & MORALS 125 (1963).
[33] Hellerstein, supra note xx, at 125.
[34] Hearings Before the Committee on Ways and Means, House of Representatives, 87th Cong., 1st Sess. on the Tax Recommendations of the President contained in his Message transmitted to Congress on April 21, 1961 at 1654 (1961) (statement of George Newman, Iowa Manufacturers Association) ("1961 House Hearings").
[35] *Expense Accounts: Firms Check Outlays Closer, Hunt Ways to Soften Tax Crackdown*, WALL ST. J., Feb. 14, 1958, at 1.

burden on their employees and effectively gross up their after-tax pay.[36] With the top marginal income tax rate at 94 percent during and immediately after the war and 91 percent between 1951 and 1963, the motivation to reduce taxable income was high. One contemporary commentator observed, "since individual taxpayers in the highest brackets have only about five CENTS of every dollar of corporate income left after federal income taxes, it is necessary to their way of life that they avail themselves of every deduction the law allows."[37] Expense accounts were an important part of this strategy, since "the executive's automobile, yacht, hunting or fishing lodge, country club membership, theater and sporting events tickets, and various other personal benefits are not included in the executive's income."[38]

Even if one company sought to resist the trend to allow their top employees to feed at the company and taxpayer-subsidized trough, there was a risk to being conservative without expense account privileges. As Russell Lynes, the managing editor of *Harper's Magazine*, observed in the *New York Times*, an employee of such a company might "leave in a huff for another company that will give him more."[39] Companies fearful of losing their best workers therefore used entertainment expense-justified items as a way to lure them to stay. "In some cases," Lynes continued, "he is supplied by the company with a house and garden and swimming pool, several cars and the service to maintain them."[40] The company rationalizes its deduction of the expenses by the fact that the employee "lives on company property and entertains for the company there" in what "is properly

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[36] Jacobs, supra note xx, at 153 (noting that the King Committee had requested that Treasury report on "attempts by some business organizations to reward key personnel with tax-free personal benefits.").
[37] S. Ralph Jacobs, *Glamorous Fringe Benefits*, B.U. L. REV. 151, 152 (1956).
[38] Norman H. Lipoff, *Entertainment and Related Expenses Under Legislative Attack*, 17 TAX L. REV. 183, 188 (1962). *See* PHILIP M. STERN, THE GREAT TREASURY RAID 113 (1964) ("Many companies have built into their pay scales liberal and non-taxable expense allowances in place of heavily-taxed salaries as a device for attracting and holding executive talent.").
[39] Russell Lynes, *Visit to the World of Expense Accounts*, N.Y. Times, Feb. 24, 1957, at 201.
[40] Lynes, supra note xx, at 201.

speaking, a dwelling maintained for what the company considers to be its business, or that part of it which goes by the name of 'public relations.'"[41]

There were countless colorful anecdotes involving companies that used expense accounts as a method of increasing after-tax compensation. In 1957, a former linoleum company executive noted that "an executive earning $50,000 a year today pays between $22,000 and $27,000 in taxes. If we gave him another $10,000 raise, he would pay still more. But if we give him $10,000 to spend on promoting our products and name, we've substantially rewarded him without penalizing him."[42] In another example involving a chemical company, one company lured away another company's executive with an offer that only matched his salary. The difference was that "the second company had some wholesalers and distributors up in Wisconsin. The man liked to fish. In his old job, he'd taken his vacation to do some fishing. Now he could visit the wholesalers for the company and nobody in the company minded if he went fishing with them. The company was delighted – and delighted to pay for his trips, too, and *still* give him a vacation."[43]

The use of the expense account in lieu of extra compensation occurred among lower-paid employees as well. Although expense accounts were still only available to a relatively small number of employees, with some estimates placing the percentage at no more than 10 percent,[44] this was still a much broader group than the executives who originated the practice. In one account, an oil company gave its top salesmen expense accounts of $700-$900 per week, as opposed to the

[41] Lynes, supra note xx, at 201.
[42] Richard Gehman, *Expense Accounts*, COSMOPOLITAN, March 1957, at 44, 45 (1957).
[43] Richard Gehman, *Expense Accounts*, COSMOPOLITAN, March 1957, at 44, 45 (1957).
[44] *See* PHILIP M. STERN, THE GREAT TREASURY RAID 111 (1964) ("Revenue officials estimate that only one taxpayer out of ten enjoys the benefits of travel and entertainment deductions.").

$125 per week normally provided to salesman, with the larger amount effectively acting as a tax-free bonus.[45]

This practice of rewarding employees with tax-free benefits was well known in government circles. In January of 1953, the House Ways and Means Committee issued a report in which it acknowledged that "recent high tax rates have resulted in attempts by some business organizations to reward key personnel with tax-free personal benefits."[46] It specifically highlighted the way in which expense accounts fit into this practice, not just because they allowed personal consumption to be financed by tax-free dollars, but because the employers openly condoned the abuse of those expenses accounts to increase their incomes, noting "the practice of allowing overly liberal expense accounts to employees whose duties involve travel or business entertainment" and "tolerat[ing] padding of the expense account by the employee as a way of giving him tax-free income."[47]

Contemporary commentators confirmed the reports' accounts of rampant expense account abuse. One observed that "it is not uncommon for a man, signing a tab in a restaurant where he is known, to put down an amount double the size of the check and take the remainder of the money for himself."[48] To demonstrate this, a writer related the story of "a well-known photographer, a gay, lively fellow with no sense whatever of personal finance, [who] once was asked how he managed to exist. 'I live on the change that waiters give me,' he said blithely."[49] Another pointed

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[45] Stern, supra note xx, at 113.

[46] Internal Revenue Investigation, Report of the Committee on Ways and Means, House of Representatives, 82d Cong., pursuant to H. Res. 78, 82d Cong., A Resolution Authorizing and Directing Certain Studies and Investigations to be Conducted by the Committee on Ways and Means 29 (Jan. 3, 1953) ("1953 House Report").

[47] 1953 House Report, supra note xx, at 29.

[48] Richard Gehman, *Expense Accounts*, COSMOPOLITAN, March 1957, at 44, 47. *See* John D. Pomfret, *"Expense Account Living" Comes Under Close Scrutiny*, N.Y. TIMES, Dec. 19, 1962, at 13 ("Sometimes cruder types padded the expense account and pocketed the difference.").

[49] Richard Gehman, *Expense Accounts*, COSMOPOLITAN, March 1957, at 44, 47.

out that "there are countless varieties of how to rig a swindle sheet that will deflate a huge income like a pricked balloon, and new ones are constantly being dreamed up by executives and their high-priced tax experts."[50]

This was perhaps the most extreme version of the common phrase that people could "live off the expense account."[51] As *The Nation* reported, "the racket has reached such proportions that in some cases it is scarcely necessary for a business executive to earn a salary – he can live like a millionaire on his expense account."[52] Noted journalist Ferdinand Lundberg claimed that "many corporation executives derive most of their take-home pay from" (1) expense accounts and (2) cut-rate stock options, "insouciantly allowing the government to clip their direct-cash salaries up to 70 percent."[53] Lundberg described one example of an executive of a corporation who was paid a salary of $25,000 that was increased in value to $98,000 because "his company paid his apartment rent, club dues and expenses (meals and drinks), entertainment expenses and an occasional trip abroad 'to study business methods overseas and improve his firm's competitive position.'"[54] It was also a practice that spread beyond the C-suite to include more than just the top executives.[55] Not only did businessmen deduct many of the daily costs of living, such as lunches, but they

[50] H.F. MILLIKIN, THE PRUDENT MAN: TAX DODGING AS AN ART 24-25 (1963) (pen name for Joachim Joesten)
[51] Malcolm Reed, *Uncle Sam v. The Expense Account*, 39 TAXES 329, 331 (1961).
[52] *High on the Hog*, THE NATION, Dec. 17, 1960, at 467.
[53] FERDINAND LUNDBERG, THE RICH AND THE SUPER-RICH 430 (1968).
[54] Lundberg, supra note xx, at 434.
[55] *See, e.g.*, William K. Zinsser, *There's No Business Like Lunch Business*, NEW YORK TIMES MAGAZINE, March 20, 1960, in U.S. Treasury Department, Study on Entertainment Expenses in President's Tax Message along with Principal Statement, Detailed Explanation, and Supporting Exhibits and Documents submitted by Secretary of the Treasury Douglas Dillon in connection with the President's Recommendations Contained in his Message on Taxation at Hearings conducted by Committee on Ways and Means, House of Representatives (May 3, 1961), Exhibit V, at 243. ("Study on Entertainment Expenses") ('Presidents of companies do not, on the whole, eat business lunches . . . But in all lower strata, business lunches are almost routine.").

deducted the costs of special events too, including "weddings, debuts and other social occasions where customers and business contacts are among the invited guests."[56]

The entrenchment of expense accounts and business entertainment spending

If the tax rates had been the only reason for the boom in expense accounts, we would have seen a marked decline in them as rates dropped. For example, the excess profits tax was repealed in 1954. That raised a corporation's after-tax cost share of entertainment expenses as a result of the elimination of the additional 30 percent rate that had previously been levied on its excess income. Nevertheless, the change "made for little, if any, cutback in the overall spending."[57] Part of the reason was that the rates had already spurred cultural and institutional changes that were not so easy to reverse.

With the growth of the expense account came the development of businesses, restaurants, night clubs, and all forms of entertainment facilities designed to take advantage of government-financed consumption.

> Wartime businessmen, spending their twenty-cent dollars, fathered a large family of new facilities which grew and prospered as the result of the travel and entertainment practices of their progenitors. During the post-war years new hotels were built and old ones expanded and modernized; the boom in restaurants, night clubs and cocktail lounges reached the proportions of a population explosion – all supported by the organization man's expense account.[58]

Although there may have been "little real relation to business" between these facilities and others, including "yachts [and] gun clubs," they were all "put on the corporate tab and written off on the

[56] Stern, supra note xx, at 112.
[57] *See I'll Just Sign: Those Big-Figure Expense Accounts*, NEWSWEEK, May 20, 1957, at 87.
[58] Michael G. Emmanuel and Norman H. Lipoff, *Travel and Entertainment: The New World of Section 274*, 18 Tax L. Rev. 487, 487 (1963).

tax form."[59] As Treasury Secretary Douglas Dillon testified before the House Ways and Means Committee in 1961, "there are few of the luxuries of life, such as vacations at fancy resorts, club memberships, and cruises which a large number of taxpayers cannot in some way deduct on tax returns as business expenses."[60] There were sometimes "serious and extensive business meetings" held in such places, but "all too often . . . the recreational activities predominate, and the business activities are so insubstantial as to constitute a sham."[61]

The expense account's influence was particularly evident in a city like New York that was both dominated by large businesses and was a destination for retail buyers for stores across the country. According to one estimate, in 1957 "some 80 per cent of luncheons served at top Manhattan restaurants like '21,' Le Pavilion and Chambord . . . are expensed."[62] During the same year, Broadway theater representatives reportedly estimated that 30 to 40 percent of all ticket sales were bought on expense accounts.[63] A decade later, little had changed. Ferdinand Lundberg estimated that the entire "New York pleasure-belt, extending roughly from 34th to 59th Streets and First to Eighth Avenues, is largely supported by expense-account deductions."[64]

Conventions were the quintessential example of an industry that literally became an institution because of the expense account. Often located in exotic places that were once the exclusive province of the wealthy few, conventions effectively offered companies the chance to reward their employees with a fantasy vacation financed largely by the government's tax subsidy

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[59] John D. Pomfret, *"Expense Account Living" Coming Under Close Scrutiny*, N.Y. TIMES, Dec. 10, 1962, at 13.
[60] Hearings before House Committee on Ways and Means on the Tax Recommendations of the President Contained in his Message Transmitted to Congress, April 20, 1961, 87th. Cong., 1st Sess. 42 (1962) (Statement of Treasury Secretary Douglas Dillon) ("Hearings on President Kennedy's Special Message")
[61] Henry Cassorte Smith, *Watch Your Expense Accounts*, 36 HARV. BUS. REV. 120, 121 (1958).
[62] Sanford Brown, *I'll Just Sign: Those Big-Figure Expense Accounts*, NEWSWEEK, May 20, 1957, at 87.
[63] *Expense Accounts: A $5 Billion Tax Deduction, and Growing*, U.S. NEWS & WORLD REPORT, Aug. 16, 1957, at 83, 86.
[64] FERDINAND LUNDBERG, THE RICH AND THE SUPER-RICH 436 (1968).

and with only a tenuous connection to business.[65] The Greenbriar, for example, a posh resort in White Sulphur Springs, West Virginia that had been the playland for presidents, diplomats, and power brokers since before the Civil War, had effectively become a convention center, with *Business Week* noting that what drew the Magazine Publishers Association to the Greenbriar in May of 1959 – in addition to the organization's annual spring meeting – was "the golf, tennis, swimming, fine food, and secluded luxury that ever since the war had been luring an increasing share of conventioneering Americans to the resort hotels."[66] Expense accounts, according to the magazine, were largely responsible for this shift:

> The America penchant for conventions – increasingly bearing the more elegant label of conferences – has reached its de luxe flowering in these rural spas that once were the exclusive domain of wealthy families and dowagers who are moving over for the growing number of expense account guests.[67]

Unlike the compensation perquisites like stock options and deferred compensation, which were primarily the exclusive province of a company's executives, conventions were a benefit available to "just about everyone in the U.S. . . . be he hod carrier, teacher, banker, or top industrialist."[68]

Not surprisingly, conventions sprung up to meet this demand. The director of the Miami Beach convention reported that convention bookings doubled between 1949-50 and 1950-51 and doubled again in 1951-52.[69] This kind of high demand for convention options continued throughout the 1950s. By the end of the 1950s, *The Economist* observed that "the annual convention is of course no novelty. For years these holiday jaunts, masked as educational meetings and therefore properly chargeable to the costs of doing business, have helped to support big resort

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[65] *See* FERDINAND LUNDBERG, THE RICH AND THE SUPER-RICH 431 (1968) (noting that "the amount of business transacted at such affairs would be hard to detect with an electron microscope.").
[66] *The Conventions – Hard Work, Hard Play*, BUS. WEEK, May 16, 1959, at 176.
[67] *The Conventions – Hard Work, Hard Play*, BUS. WEEK, May 16, 1959, at 176-78.
[68] *The Conventions – Hard Work, Hard Play*, BUS. WEEK, May 16, 1959, at 178.
[69] Hal Foust, *Tax Deductions Can Pay for Trip to Sunny South*, CHI. DAILY TRIB., Feb. 22, 1952, at B4.

hotels with convenient golf courses attached."[70] The entertainment aspect of the deductible convention business became so significant that some groups looked for venues where they could get attendees to focus on work a bit more. According to the Furness Bermuda Line, for example, the percentage of its cruise bookings attributed conventions jumped from 18 percent in 1958 to 26 percent in 1959, an increase attributed to the fact that ther "are no golf courses attached" to cruise ships at sea.[71]

As conventions, annual sales meetings, and industry trade associations multiplied, it became simple for the average taxpayer to find a suitable business excuse from which to leverage a family vacation. Indeed, it became clear that you were a chump if you did otherwise. Hal Foust, a columnist for the *Chicago Daily Tribune*, writing from Miami Beach, exclaimed that "if you haven't contrived a business trip to this playground, you're missing something. That's the way more and more smart operators are paying for visits here – classifying travel and hotel bills as business expenses deductible as such on income tax returns. Uncle Sam, in other words, is catching more and more of the checks around here."[72] The organizers of these meetings were all too willing to accommodate this desire for deductible pleasure trips. One vice-president of an insurance company that was holding an annual meeting in Fort Monroe, Virginia wrote the hotel manager in search of recommendations for side trips, admitting that "while we hold two business sessions during our four-day convention, business is secondary. The main object is to give our people a good time. Specifically, I would be interested in knowing the fishing accommodations . . ."[73]

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[70] *Life at Uncle Sam's Expense*, THE ECONOMIST, April 18, 1959, at 234, 235.
[71] Id. At 235.
[72] Hal Foust, *Tax Deductions Can Pay for Trip to Sunny South*, CHI. DAILY TRIB., Feb. 22, 1952, at B4.
[73] Stern, supra note xx, at 114-15.

Some companies went beyond funding conventions to literally creating vacation resorts to be used by their employees. In one example, the Slaymaker Lock Company of Lancaster, Pennsylvania, acquired a farm and the stone house that was located on the property in 1943 and then spent almost three times the price to improve the property and turn the house into a "recreation lodge."[74] The company then conveyed the property to a trust controlled by an association of the foreman of the company. Under the trust, the property was to be maintained for the exclusive use and enjoyment of the employees, which the Tax Court held in 1952 to be sufficient to classify it as a deductible business expense. According to the court, "petitioner's volume of business more than quadrupled what it had been during the prewar years." Since it "had to compete with other industries in the area likewise engaged in war activities" and its wages were largely fixed by the wartime wage stabilization regulations, it used the recreation lodge "as a means of holding old employees, to attract new employees, and to cut down its labor turnover."[75] The court may have been fooled by the taxpayer in this and other similar cases. As one commentator noted, "ostensibly" these properties were used employees, but they "actually [were] for the use of a key stockholder-officer as a country home. An annual barbeque picnic for the employees is staged in the hope that such a red herring will cause the Internal Revenue Service to lose the scent."[76]

There were dozens of variants on the vacation resort used by companies to create tax deductible opportunities to reward employees and entertain customers, including things like yachts, hunting lodges, and fishing camps. Business owners also went to great extents to dress up their vacation expenses as business-related. Ray Kroc, the late owner of the fast food franchisor

[74] Slaymaker Lock Company, 18 T.C. 1001 (1952).
[75] Id.
[76] Henry Cassorte Smith, *Watch Your Expense Accounts*, 36 HARV. BUS. REV. 120, 121 (1958).

McDonald's corporation, bought a large ranch in Santa Ynez, California in the mid-1960s after the company held an initial public offering and he instantly became a multi-millionaire.[77] Kroc had apparently fallen in love with the area while on vacation, envisioning it as a vacation spot for himself and other McDonald's executives, but, apparently at the advice of his tax counselors seeking to shelter some of his income and the gain he had made in the IPO, he also established a test kitchen (a "research and development facility") and the headquarters for his newly-created foundation, there.[78] Stanley Ruttenberg of the AFL-CIO testified before the House Ways and Means Committee about another example involving "an alleged business-connected expenditure" involving a "cake and cookie bakery's $18,000 to $26,000 annual deduction for a yacht used exclusively to entertain supermarket and chainstore buyers on deep sea fishing trips."[79] As Ruttenberg remarked, it was likely that "they caught very few cookies from that yacht."[80] A more egregious example, according to Ruttenberg, was $666,000 worth of deductions taken collectively by three manufacturers over a six-year period for the shared expenses maintaining a hunting lodge and duck-hunting preserve.[81]

For the companies that were uncomfortable with owning resort property or with justifying it as a business expense, they instead created a business justification for resort travel. In 1957, the Internal Revenue Service advised field agents that "one area which requires close attention involves the use of alleged branch offices in resort cities for the sole purpose of sending business

[77] Lisa Napoli, *The Ranch that Big Macs Built*, LA CURBED, Nov. 17, 2016, available at https://la.curbed.com/2016/11/17/13629490/mcdonalds-founder-ray-kroc-california (last visited 11/9/2020).
[78] Id.
[79] Hearings Before the Committee on Ways and Means, House of Representatives, 87th Cong., 1st Sess. on the Tax Recommendations of the President contained in his Message transmitted to Congress on April 21, 1961 at 1651 (1961) ("1961 House Hearings").
[80] Id.
[81] 1961 House Hearings, supra note xx, at 1651 (statement of Stanley Ruttenberg, Research Director, AFL-CIO)

executives to such cities for vacation."[82] According to one account, it was "a growing practice . . . for a small firm to maintain an unused office as a 'front' in a resort area."[83] This "phony branch office . . . gives executives an excuse to deduct travel expenses for visits ostensibly made to the branch office."[84] In reality, however, "these visits can be a cloak for personal vacation trips."[85]

Expense Account Envy and Outrage

It was an open secret that expense accounts were a catch-all for tax avoidance. Indeed, a common nickname for the expense account was a "swindle sheet."[86] One columnist for the *New York Times* called the expense account "one of the uneasy national jokes of our time . . . it has become one of the greenest of playing fields for that all-American exercise in sportsmanship, getting around the income tax."[87] Under what some described as "expense account morality . . . a company has a lodge to entertain customer-executives in the South Sea Isles. Or there's a yacht for meetings of the board of directors. Or duck-hunting blind with bar attached. Or airplanes to whisk men away to pleasure dates as well as business dates."[88] One Internal Revenue Service agent described myriad potentially abusive "items that turn up regularly on expense accounts," including "upkeep of their homes, entertainment in their homes, clothes for their wives, and services provided for business associates – services such as furnishing chartered planes or railroad

[82] I.R.-Circular No. 57-85 (June 20, 1957).
[83] *Expense-Account Scandal*, U.S. NEWS & WORLD REPORT, Jan. 25, 1960, at 50, 52.
[84] Id.
[85] Id.
[86] Richard Gehman, *Expense Accounts*, COSMOPOLITAN, March 1957, at 44.
[87] Russel Lynes, *Visit to the World of Expense Accounts*, N.Y. TIMES, Feb. 24, 1957, at 201.
[88] J.A. Livingston, *Business Outlook: Wives Can Be Tax Deductible*, WALL ST. J., May 2, 1956, at 27.

cars, limousines and chauffeurs, or supplying private secretaries complete with typewriters and dictating machines."[89]

What differentiated expense account abuse is that it was not limited to the super rich. As one contemporary commentator put it, "at the very top of the social pyramid" of billionaires and demi-billionaires, "tax-dodging is often looked upon as a sort of sport," but "in the next-to-highest brackets . . . tax evasion is cultivated as a fine art, if not an exact science," citing expense accounts as "a real 'old faithful' in this game."[90] William Graham Balter, a Los Angeles lawyer and the author of a 1953 treatise on tax fraud, cited "padding of business entertainment expenses" as one example of "tax evasion unfortunately practiced on a wide scale by rich and poor alike."[91]

Business interests protested that the reports of expense account abuse appeared to exaggerate the magnitude of the problem. As Clarence Randall, a former chairman of Inland Steel Company and an adviser to Presidents Dwight Eisenhower and John F. Kennedy observed, "this orgiastic abuse of the expense account is by no means universal, or even in a broad sense characteristic of our business community today."[92] Henry Rothschild, speaking as part of the House Ways and Means Committee's Panel on Income Tax Revision in favor of expense account reform, conceded that "there is some disagreement among members of this panel as to the existence of a real expense account problem. Certainly the published statistics are based on pure

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[89] Gehman, supra note xx, at 45.
[90] H.F. MILLIKIN, THE PRUDENT MAN: TAX DODGING AS AN ART 24 (1963).
[91] HARRY GRAHAM BALTER, FRAUD UNDER FEDERAL TAX LAW 16 (2d ed. 1953).
[92] Clarence B. Randall, *The Myth of the Magic Expense Account*, DUN'S REV., Aug. 1960, at 39, 40. This excerpt was reprinted in U.S. Treasury Department, Study on Entertainment Expenses in President's Tax Message along with Principal Statement, Detailed Explanation, and Supporting Exhibits and Documents submitted by Secretary of the Treasury Douglas Dillon in connection with the President's Recommendations Contained in his Message on Taxation at Hearings conducted by Committee on Ways and Means, House of Representatives (May 3, 1961), Exhibit V, at 237. ("Study on Entertainment Expenses")

estimates, and hearsay rather than true research."[93] Edward Schlaudt a corporate attorney who also participated in the Panel on Income Tax Revision, protested that "on the basis of my own experience . . . I refuse to believe that there is really any significant expense account abuse merely because there have been some loose charges and lurid magazine articles in the last few years."[94] In part, Schlaudt's logic rested on the fact that companies had good reasons to scrutinize expense account spending, given the pressure from stockholders to increase profits.[95] After all, if it did not make good business sense to permit lavish expense accounts, a deduction, even at the high post-World War II income tax rates applicable to corporations, was not likely to make sense either. Even Randall, however, conceded that it was "a spectacular and alarming trend, participated in by enough companies and individuals to put all of us upon caution for the good reputation of business men as a class."[96]

The Internal Revenue Service tended to agree that the problem was not as bad as it might seem. Dana Latham, who had been appointed Commissioner of Internal Revenue in 1958, conceded while speaking at a meeting of the Tax Executives Institute in 1959 that "while the Service obviously cannot determine with certainty the full extent of this problem, indications at hand would imply that these criticized practices are not nearly as widespread as this publicity suggests."[97]

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[93] Income Tax Revision: Panel Discussion before the House Committee on Ways & Means, House of Representations, 86th Cong., 1st Sess., Ideas and Suggestions Submitted to the Committee on Ways and Means on the Broad Subject of the Revision of the Federal Income Tax Structure, Dec. 2, 1959, at 587 (testimony of Henry Rothschild).
[94] Income Tax Revision, *supra* note xx, at 590 (testimony of Edward J. Schlaudt).
[95] Id. at 590-91.
[96] Clarence B. Randall, *The Myth of the Magic Expense Account*, DUN'S REV., Aug. 1960, at 39, 40.
[97] Dana Latham, *The Internal Revenue Service: Recent Developments and Some Current Problems*, 12 TAX EXECUTIVE 7, 11 (1959).

Even if complaints about expense account abuse were a bit overblown, many of the stories were outlandish and made for good copy, leading them to spread widely. As one accountant argued, "the so called expense account abuses became fashionable subjects for cartoonists, columnists and feature writers. Through such mediums the man on the street has probably been led to believe that the extreme cases he reads about are comnmonplace and typical."[98] Henry Rothschild, City Attorney for New York, testified before the House Ways and Means Committee that "these cases are so flamboyant and resultant expense account publicity has been so sensational that in my view a fresh new program is indicated to prevent a breakdown of our self-assessment system."[99]

These reports gave the average person a peak into the heretofore unknown world of expense accounts. Treasury noted in a 1961 report that "the millions of taxpayers who are not so fortunate as to have an expense account . . . are reading and hearing more and more of expense-account abuses."[100] The report explained that "the portrait presented by these articles is that of a privileged class which has become known as the 'expense-account society' – a society made up of individuals who, because of the liberality of our tax laws, practically live on expense accounts."[101]

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[98] B. Kenneth Sanden, *Guidelines for Handling the Reporting of Business Expenses and Reimbursements*, 38 TAXES 972, 972-73 (1960).

[99] Income Tax Revision: Panel Discussion before the House Committee on Ways & Means, House of Representations, 86th Cong., 1st Sess., Ideas and Suggestions Submitted to the Committee on Ways and Means on the Broad Subject of the Revision of the Federal Income Tax Structure, Dec. 2, 1959, at 587 (testimony of Henry Rotschild) ("Income Tax Revision").

[100] U.S. Treasury Department, Study on Entertainment Expenses in President's Tax Message along with Principal Statement, Detailed Explanation, and Supporting Exhibits and Documents submitted by Secretary of the Treasury Douglas Dillon in connection with the President's Recommendations Contained in his Message on Taxation at Hearings conducted by Committee on Ways and Means, House of Representatives (May 3, 1961), Exhibit V, at 236. ("Study on Entertainment Expenses")

[101] Study on Entertainment Expenses, supra note xx, at 236.

The well-publicized examples of expense account abuse served to normalize the practice. Commentators even compared the prevailing climate to Prohibition in that "bad laws produce bad men. Even good men, in a bad moral climate, are inclined to lose their ethical orientation."[102] In a 1958 speech to the Tax Executive Institute, Under Secretary of the Treasury Fred Scribner echoed these sentiments, calling expense account abuse "a matter of business morality."[103] One columnist noted that when government officials, professional men, and corporation officials engage in self-serving practices, and use the expense account to raise their standards of living at taxpayer expense, they bring down on themselves not only censure," but the tax structure itself.[104] "If they shrink from paying taxes, if they condone misapplication of the expenses account, why shouldn't everyone?"[105] Another noted that the "laboring man is as willing to falsify his tax return as his richer brother," suggesting that the "social pressure" to avoid taxes is like a repeat of prohibition.[106]

Although the news reports of expense account abuses induced some to join in, for others who were unable or unwilling to do so, they only served to fan the flames of discontent. As Lucius Beebe, a columnist with the *San Francisco Chronicle* observed, the lavish and unnecessary expenditures "is the aspect of expense account civilization that is most distasteful to people of ordinary means and prudent ways with money, even if they have it an ample abundance. . . . [big businesses] make more enemies among a class of people naturally sympathetic to corporate

[102] Livingston, supra note xx, at 27.
[103] Remarks by the Under Secretary of the Treasury Scribner, February 17, 1958, Tax Executive Institute, Washington, D.C., in Annual Report of the Secretary of the Treasury on the State of the Finances for the Fiscal Year ended June 30, 1958, exh. 56, at 345.
[104] J.A. Livingston, *Business Outlook: Adams' Plight Symbol of our Amoral Times*, WASH. POST AND TIMES HERALD, June 20, 1958, at B9.
[105] Livingston, Adams' Plight, supra note xx, at B9.
[106] Rene A. Wormser, *The Third American Revolution: A Reform Movement Gone Wrong*, 39 A.B.A. J. 389, 439 (1953).

vastness than all the radical agitators and socialists put together."[107] These observations may have led a writer in the *New York Times Magazine* to observe that "seen from a distance, the group portrait of expense-account society presents a rather curious picture. To a great many people, it inevitably looks and will continue to look like the *society of kept men*."[108]

Expense account living may have been a cause for envy by itself, but what really disturbed the average person was that this luxury was indirectly financed by themselves as taxpayers. As lawyer and novelist Louis Auchincloss remarked in a letter to the editor in the *New York Times*, "the vice of the system is . . . in the privilege of a few to dine and wine at the expense of the taxpayer."[109] Russell Lynes expressed a similar sentiment, lamenting that "the tax structure seems to create one ethic for certain business men whose services are greatly in demand by corporations and another for the rest of us . . . [Such business man] looks slightly ridiculous to a great many of us, for it is we who in the long run pay our taxes to keep him in the style to which he would like to become accustomed."[110]

Some taxpayer resentment related to the effect that taxpayer-financed luxury spending had on the prices ordinary people had to pay for similar consumption.[111] Beebe blamed expense accounts for pricing out the average person from plane travel and hotels, predicting that "without expense accounts . . . the fares would be down within reach of folks with perhaps some reasonable justification for travel" and "the same would be true at luxury hotels" where suites "would be down to the $10 they are worth if free-loading executives as a class were turned out of them bodily and

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[107] Lucius Beebe, *Expense Account Caviar*, SAN FRAN. CHRON., March 20, 1961, at 36.
[108] Hellerstein, supra note xx, at 126.
[109] Louis Auchincloss, *Letter to the Editor, Deductions for Entertaining*, N.Y. TIMES, Dec. 6, 1960, at 40.
[110] Russell Lynes, *Visit to the World of Expense Accounts*, N.Y. TIMES, Feb. 24, 1957, at 201.
[111] Norman H. Lipoff, *Entertainment and Related Expenses Under Legislative Attack*, 17 TAX L. REV. 183, 187.

en masse."[112] The theory was that "the spendthrift attitude of those who are paying only a portion of the cost as a result of the business expense deduction," led to a degree of price insensitivity that permitted establishments to raise their prices.[113] As a result, "critics charge that the interaction of expense account habits and income tax rules distorts the price system and weakens the moral fibre of the country. The evidence offered includes such trends as the climbing prices of beefsteaks and theatre tickets."[114] Beefsteaks were reportedly unavailable in New York because they were all "being eaten in Chicago by business men attending conventions on expense accounts," while "the most popular New York plays are sold out weeks in advance because corporations in Detroit and Pittsburgh buy up blocks of seats and issue them to officers making business trips to New York, or to salesmen needing to entertain important customers there."[115] Representative Al Ullman, an Oregon Democrat and future chair of the House Ways and Means Committee, confirmed these anecdotes, noting that "it has been my experience that the average citizen traveling on his own money is pretty well priced out of the market when it comes to big city nightclubs, some hotels, and other types of amusement, because those are living pretty much on expense account money and it has a very definite inflationary effect on our economy."[116]

Such discontent grew stronger when families of average means saw the abusive behavior up close. One "taxpayer in the moderate income bracket" relayed an anecdote that illustrated how the unequal distribution of expense accounts created problems:

> My neighbor has a big expense allowance. Every now and then he invites my wife and me to dinner and the theater. Sometimes he takes our boy along with his own son to a baseball

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[112] Lucius Beebe, *Expense Account Caviar*, SAN FRAN. CHRON., March 20, 1961, at 36.
[113] Lipoff, supra note xx, at 187.
[114] *Life at Uncle Sam's Expense*, THE ECONOMIST, April 18, 1959, at 234-35. See Lipoff, supra note xx, at 187
[115] *Life at Uncle Sam's Expense*, THE ECONOMIST, April 18, 1959, at 235.
[116] Hearings Before the Committee on Ways and Means, House of Representatives, 87th Cong., 1st Sess. on the Tax Recommendations of the President contained in his Message transmitted to Congress on April 21, 1961 at 1611 (statement of Rep. Al Ullman, D-Ore.) (1961) ("1961 House Hearings")

> game. When we protest at the cost he says, "Don't give it a thought. Uncle Sam is paying for it." The catch comes when we try to reciprocate. I have no big expense account. When we entertain this man in return, it comes out of our own pockets. We simply can't afford to entertain as lavishly as he does.[117]

Clarence Randall explained how this "rising public indignation" over lavish expense account living arises from the envy of those who lacked expense accounts for those who had them:

> An ordinary fellow – say, an executive from a public utility where every penny is scrubbed before it is spent – takes his wife out to dinner for the one big evening of the year. He finds at the next table a neighbor who has just ordered his third bottle of champagne, although he is known to be two payments behind on his car. And the ordinary decent citizen doesn't like what he sees. He cannot deduct his wife's dinner from his personal income tax as an expense, and he resents watching someone else live it up for free. So, when they hear about it second-hand from waiters and hat-check girls, do teachers and policemen and others who have just had a pay raise denied. So do I. And so does anyone else who understands and values the free enterprise system."[118]

The real problem was not that people envied those who were wealthier than they were, but rather that people who were no wealthier than they were got to act like they were wealthy. As Norman Lipoff observed, "expense account spending creates a group in our society which appears wealthy not primarily because they have money, but because they are able to spend it."[119]

Some taxpayers, angry with expense account abuses, took matters into their own hands to try to stem the practice. According to a field agent in Detroit, "one thing that reassures us is that we get from 200 to 250 letters a month from people who say something like 'I pay my taxes but so-and-so down the street told me he didn't pay taxes on such-and-such.'"[120] The agent continued, "these people aren't being snoopy. They're downright indignant that they're carrying their load and others aren't." These efforts did not fall on deaf ears. The U.S. News & World Report attributed an IRS crackdown on expense account abuse on "the rising number of complaints from

[117] *Expense-Account Scandal*, U.S. NEWS & WORLD REPORT, Jan. 25, 1960, at 50.
[118] Clarence B. Randall, *The Myth of the Magic Expense Account*, DUN'S REV. Aug. 1960, at 39, 40.
[119] Lipoff, supra note xx, at 187.
[120] *Tax Dodgers: Stiffer Enforcement Deters Some Cheaters, But Many Persevere*, WALL ST. J., April 11, 1957, at 1.

taxpayers who do not have expense accounts, and are irked by the ostentatious living of some of those who enjoy expense deductions."[121]

This growing outrage may be why Robert Lubar, who went on to become managing editor of Fortune Magazine, wrote in 1959 that "the form of income concealment that most concerns the Treasury today is the abuse of deductions for business expenses."[122] According to Lubar, "what bothers the revenue collectors is not only the revenue that is lost by excessive or illegitimate deductions but, more important, the effect on the morale of taxpayers who have no expense accounts and feel they are getting a raw deal." Others echoed these sentiments, suggesting that "what concerned [the Government] was the moral issue and the very practical question of the effect on the nation's tax system, which relied upon self-reporting and self-assessment, if the idea became widespread that it was smart to beat the game."[123]

As a result, these "lurid news accounts of tax-supported yachts and hunting lodges stirred a movement toward expense account reform."[124] As Clarence Randall pointed out, "an attack on business is sure-fire in many Congressional districts. Nothing goes over better than to expose special privilege which is not available to the ordinary citizen. All that Congress has to do is move in and pass a bill limiting the right to deduct entertaining as a business expense and it will be finished."[125]

[121] *Expense-Account Scandal*, U.S. NEWS & WORLD REPORT, Jan. 25, 1960, at 50.
[122] Robert Lubar, *A Plan for Tax Reform*, FORTUNE, March 1959, at 92, xx.
[123] John D. Pomfret, *"Expense Account Living" Coming Under Close Scrutiny*, N.Y. TIMES, Dec. 10, 1962, at 13.
[124] Stern, supra note xx, at 116.
[125] Clarence B. Randall, *The Myth of the Magic Expense Account*, DUN'S REV. Aug. 1960, at 39, 40.

Some went a step further than Randall predicted and called for the elimination of the deduction for entertainment expenses altogether.[126] The rebuttal was that it would be difficult to distinguish between personal and business-related entertainment and we would end up over-taxing by not allowing a deduction for the business-related portion of the expenses.[127] New York University law professor Harry Rudick testified to the Income Tax Revision Panel that although "it is well known that one of the most prevalent tax avoidance techniques is the expense account," he characterized "the problem [as] simply one of abuse."[128] According to Rudick, "incidental entertainment is a common and productive event in business life, and there should be no question as to legitimate entertainment expenses."[129]

Treasury Enforcement Efforts

Treasury's initial response to reports of expense account abuse was to ramp up enforcement efforts. In an Internal Revenue Service Circular distributed in 1957 to field agents conducting audits, the agency noted that "for some time our field agents have been alerted to abuses by income taxpayers in claiming deductions for travel and entertainment which could not be justified as ordinary and necessary business expenses."[130] As a consequence, the Circular continued, "we have been taking a close look at expense deductions claimed involving such items as club dues,

[126] Henry Rothschild & Rudolf Sobernheim, Expense Accounts for Executives, 67 Yale L.J. (1958); Income Tax Revision: Panel Discussion before the House Committee on Ways & Means, House of Representations, 86th Cong., 1st Sess., Ideas and Suggestions Submitted to the Committee on Ways and Means on the Broad Subject of the Revision of the Federal Income Tax Structure, Dec. 2, 1959, at 582.
[127] Income Tax Revision, supra note xx, at 582.
[128] Income Tax Revision, supra note xx, at 588.
[129] Income Tax Revision, supra note xx, at 588.
[130] I.R.-Circular No. 57-85 (June 20, 1957).

entertainment, travel, maintenance of automobiles, yachts, and airplanes, maintenance of company-supported residences, and so forth."[131]

Russell Harrington, the Commissioner of Internal Revenue, underscored the red flag status of expense account deductions in a speech delivered at Brown University on September 5, 1957.[132] Harrington identified "the accounting for blanket expense account allowances by employers" as a particular "trouble spot," noting that they "may raise questions of actual, verifiable expenses of the recipient as against additional compensation to him."[133] The Internal Revenue Service was particularly troubled with "the increasing tendency to misstate, 'pad,' and even cheat" on their expense accounts, effectively reducing tax revenues and effectively "placing a burden on the honest taxpayer."[134] Harrington went on to mention "dubious instances that have come to our attention include deductions, as expenses, of purported business trips by executives vacationing at resort hotels, expenses of hunting trips, expenses of attending sporting events in distant cities, and for other non-business expenses under the guise of business trips."[135]

This campaign to crackdown on expense account abuse became more focused by the early 1960s. In April 1960, Dana Latham, the Commissioner of Internal Revenue, announced a comprehensive travel and entertainment enforcement initiative.[136] It was not a change to existing law, but it required disclosures that might have had a chilling effect on taxpayers seeking to deduct such expenses. This required the inclusion of "(1) an expense account schedule for certain officers, partners and highly-paid employees, and (2) a questionnaire concerning hunting lodges, yachts,

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131 I.R.-Circular No. 57-85 (June 20, 1957).
132 How Income Tax Returns are Audited, 1957 Standard Fed. Tax Rep. 52001, ¶8646, at 54,809 (1957).
133 How Income Tax Returns are Audited, 1957 Standard Fed. Tax Rep. 52001, ¶8646, at 54,809 (1957).
134 Henry Cassorte Smith, *Watch Your Expense Accounts*, 36 HARV. BUS. REV. 120 (1958).
135 How Income Tax Returns are Audited, 1957 Standard Fed. Tax Rep. 52001, ¶8646, at 54,809 (1957).
136 Mortimer R. Caplin, *The Travel and Entertainment Expense Problem*, 39 TAXES: THE TAX MAGAZINE 947, 949 (1961).

apartments, conventions and similar items."[137] The following year, the Secretary of the Treasury submitted a report to Congress providing some of the details the Internal Revenue Service had learned from its study of the travel and entertainment expense issue based on audits over a three month period, including its finding that nearly half of all returns claiming travel and entertainment expense deductions contained errors.[138]

There was evidence that these enforcement initiatives efforts had at least some effect. Businessmen, according to a *Wall Street Journal* survey conducted in 1962, reported that the "use of these tax-deductible accounts as 'swindle sheets' is declining," in part because of the "concerted campaign" IRS agents began in 1960 "to scrutinize expense-account deductions more closely."[139] Nevertheless, even after "a decade of administrative effort" to "ferret out the unwanted expenses,"[140] IRS Commissioner Mortimer Caplin observed that the problem "remain serious."[141]

One of the reasons that expense account abuse seemed resistant to enforcement efforts was that even where auditors successfully identified questionable deductions, courts often nullified them by what some considered "an all too generous conception of where the line should be drawn between personal and business expense."[142] In one infamous example, Mr. and Mrs. O Carlyle Brock, the owners of Sanitary Farms Dairy, deducted the entire cost of an African safari as an advertising expense for their business.[143] Boarding a plan in Erie, Pennsylvania on May 28, 1950, the Brocks first made stops in London, Paris, and Rome – taking motion pictures in each -- before heading to Africa to a "big game hunt" where they reportedly "killed a number of an imals" and

137 Caplin, The Travel and Entertainment Expense Problem, supra note xx, at 949.
138 Caplin, supra note xx, at 951-52.
139 *Expense Accounts- New Tax Rules Likely to Further Cut Abuses*, WALL ST. J., Oct. 11, 1962, at 1.
140 Caplin, supra note xx, at 953; Hellerstein, supra note xx, at 129.
141 Caplin, supra note xx, at 964.
142 Hellerstein, supra note xx, at 129.
143 Sanitary Farms Dairy, Inc. v. Commissioner, 25 T.C. 463 (1955).

captured several, including a tiger and two leopards for the Erie Zoo, all the while filming portions of their trip before returning in November of 1950.[144] Upon their return, the couple put together an edited film of their trip and invited wholesale customers and others to their farm to watch it and to tour the facility where their game trophies were displayed.[145] Although the court conceded that "the cost of a big game hunt in Africa does not sound like an ordinary and necessary business expense of a dairy business in Erie, Pennsylvania," it found in favor of the taxpayers.[146] Perhaps anticipating the obvious objections, the judge wrote that while the couple "admittedly enjoyed hunting, . . . enjoyment of one's work does not make that work a mere personal hobby or the cost of a hunting trip income to the hunter. There is evidence that this trip represented hard work on the part of the [taxpayers], undertaken for the benefit of the Dairy, rather than as a frolic of their own."[147] As NYU Law Professor Jerome Hellerstein sarcastically noted when commenting on this portion of the opinion, "it was purely coincidental that the president loved to hunt big game."[148]

The Sanitary Farms case was often cited as evidence of the futility of using increased auditing to rein in the abuses of entertainment deductions. The Internal Revenue Service complained that "when existing law allows the cost of a safari to Africa, undertaken by a hunting enthusiast and his wife, to be deducted on the ground that it provides advertising for dairy milk, one cannot expect revenue agents to successfully question the business necessity of duck hunting or night-clubbing with business associates."[149]

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[144] Daniel Candee Knickerbocker, Jr., *Entertainment and Related Deductions Under the Revenue Act of 1962*, 31 FORDHAM L. REV. 639 (1963).
[145] Sanitary Farms Dairy, Inc. v. Commissioner, 25 T.C. 465-66 (1955).
[146] Id. at 467.
[147] Id. at 468.
[148] Hellerstein, supra note xx, at 130.
[149] Daniel Candee Knickerbocker, Jr., *Entertainment and Related Deductions Under the Revenue Act of 1962*, 31 FORDHAM L. REV. 639, 640 (1963) (quoting Hearings on the Tax Recommendations of the President Before the House Committee on Ways and Means, 87th Cong., 1st Sess. 166 (1961)).

Even if Treasury's stricter auditing had been effective, it only covered businesses since the individuals who were the beneficiaries of the expense accounts did not have to disclose that on their own returns. In 1958, the Internal Revenue Service sought to remedy this by adding line 6-A to individual income tax returns, which asked taxpayers to list how much they receive for business expenses upon which they paid no taxes.[150] This had been required as early as 1921 , but had been dropped from income tax forms in 1944.[151] The target for reviving it was reportedly "the high-living, free-spending taxpayers who have used tax-free allowance income to live higher and to spend more."[152] Opponents charged that the change was made too late in the year and "taxpayers claimed it would be too difficult to go back and reconstruct their records," so it was delayed.[153] According to the *Wall Street Journal*, "after a howl from confused taxpayers, the I.R.S. backtracked a bit and said not to fill out the line on the 1957 forms. But it warned the ruling would stick for 1958 personal income tax reports."[154] This return, however, never happened. Apparently, the attempt to shift the responsibility to the individual with an expense account "to justify all of his business spending . . . touched a tender political nerve [and] the resulting reaction forced abandonment of the plan."[155]

Legislative Action

When administrative efforts failed or proved too controversial, reformers transitioned to legislative reforms. In theory, the government might have responded to the motivation to stretch the limits of the entertainment deduction by reducing the progressivity of the income tax and

[150] Alvin Shuster, *Expense Account Gets Top Billing*, N.Y. TIMES, Jan. 1, 1958, at 17.
[151] Shuster, supra note xx, at 17.
[152] Shuster, supra note xx, at 17.
[153] Malcolm Reed, *Uncle Sam v. The Expense Account*, 39 TAXES 329, 331 (1961).
[154] *Expense Accounts: Firms Check Outlays Closer, Hunt Ways to Soften Tax Crackdown*, WALL ST. J., Feb. 14, 1958, at 1.
[155] *Expense-Account Scandal*, U.S. NEWS & WORLD REPORT, Jan. 25, 1960, at 50.

therefore the benefits of the deductions.[156] As Rudick explained, if a corporate executive's tax bracket was reduced from 90 percent to 60 percent, "he would be less likely to suggest to his employer corporation that instead of giving him a raise, they should supply and maintain for him a city apartment."[157]

Instead of addressing the incentives for pursuing questionable deductions, reformers focused on trying to the confine the deductible amounts to the business-related expenses.[158] President John F. Kennedy's 1961 tax message to Congress specifically targeted the "widespread abuse" of expense accounts.[159] He argued that "too many individuals have devised means of deducting too many personal living expenses as business expenses, thereby charging a large part of their cost to the Federal Government."[160] Bemoaning the fact that "expense account living has become a byword in the American scene," Kennedy vowed that "the slogan – 'It's deductible' – should" be eliminated from the lexicon.[161]

Under Kennedy's proposal, entertainment expenses, defined to include expenses on "the amusement, recreation, or similar pleasurable diversion of any individual," would be completely non-deductible, as would expenses on facilities used primarily for those purposes and club dues

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[156] *See* Income Tax Revision, supra note xx, at 589 (statement of Harry Rudick) ("the unnecessary and unwise – in my opinion – range of progression in the upper individual tax brackets contributes significantly to the problem of entertainment and travel expenses."); Norman H. Lipoff, *Entertainment and Related Expenses Under Legislative Attack*, 17 TAX L. REV. 183, 188 (1962) ("The high progressive tax rate is undoubtedly a major impetus to the use and abuse of expense accounts, for it eliminates a tax on what would otherwise be compensation. Similarly, those not on expense accounts are tempted by the high progressive rates to spend on entertainment, since the out-of-pocket costs is comparatively low.").
[157] Income Tax Revision, supra note xx, at 589.
[158] The Senate actually passed a measure designed to restrict expense account deductions, but it died in the House and Congress instead directed the Internal Revenue Service to conduct further study of the issue. PHILIP M. STERN, THE GREAT TREASURY RAID 116 (1964).
[159] President John F. Kennedy's Special Message to Congress on Taxation, April 20, 1961.
[160] President John F. Kennedy's Special Message to Congress on Taxation, April 20, 1961.
[161] President John F. Kennedy's Special Message to Congress on Taxation, April 20, 1961.

for "social, athletic, or sporting clubs or similar organizations."[162] Treasury Secretary Dillon indicated that this would include expenses for "entertaining guests at nightclubs, theaters, country clubs, prizefights, and on hunting and fishing trips."[163] It would also bar a deduction for spending on more mundane things, such as "automobiles, airplanes, apartments, and hotel suites" to the extent they were used "as a substitute for personal living and family expenses."[164]

Meals and beverages posed particularly thorny problems for reformers eager to police the personal/business borderline. As the authors of a treatise on executive compensation asked, "[e]very executive and his family must eat; but should the entire cost of a dinner, often more elaborate than usual, become a tax deduction because a business guest is entertained at the table?"[165] "Or," the authors continued, "should the deduction be limited to the amount attributable to the guest's share of the meal or to the shares of both the guest and the executive? Or should a deduction for the host be limited to the difference between the cost of his ordinary dinner and the more elaborate dinner of which partakes because of the business guest?"[166] These were the types of questions that had been raised by the Tax Court in a 1953 case, *Sutter v. Commissioner*:

> When a taxpayer in the course of supplying food or entertainment or making other outlays customarily regarded as ordinary and necessary includes an amount attributable to himself or his family, such as the payment for his own meals, is that portion of the expenditure an ordinary and necessary business expense on the one hand or a nondeductible personal item on the other?[167]

[162] Hearings before House Committee on Ways and Means on the Tax Recommendations of the President Contained in his Message Transmitted to Congress, April 20, 1961, 87th. Cong., 1st Sess. 73-74 (1962) (Statement of Treasury Secretary Dillon) ("Hearings on President Kennedy's Special Message").
[163] Hearings on President Kennedy's Special Message, supra note xx, at 73 (Statement of Treasury Secretary Dillon).
[164] Hearings on President Kennedy's Special Message, supra note xx, at 73.
[165] Henry Rothschild & Rudolf Sobernheim, *Expense Accounts for Executives*, 67 YALE L.J. 1363, 1379 (1958).
[166] Rothschild & Sobernheim, supra note xx, at 1379.
[167] Sutter v. Commissioner, 21 T.C. 170, 173 (1953).

In *Sutter*, the court resolved those questions by splitting the difference, noting that expenses for meals for oneself and one's dependents "is ordinarily and by its very nature personal expenditures forbidden deduction" under the Code.[168] Given this, the court created a rebuttable presumption that "may be overcome only by clear and detailed evidence as to each instance that the expenditure in question was different from or in excess of that which would have been made for the taxpayer's personal purposes."[169]

Food and beverages were also non-deductible under Kennedy's proposal, but subject to three exceptions that were designed to more narrowly stake out the personal-business boundary line. One was for meals provided to employees on the business premises of the employer.[170] A second was for expenses for food and beverages incurred while traveling away from home on business, but only with respect to the portion of the trip that was related to its business purpose.[171] The third exception related to the most common and hard to police situation, and therefore it was the most complex. This was for food and beverages provided as part of a business meeting, but only if the meeting involved "discussions or similar activities which are directly related to the operation of the taxpayer's business and which are not furnished for the principal purpose of creating good will."[172] This would effectively disallow "cocktail parties and other functions which are primarily of a social or entertainment character for the purpose of creating good will."[173] Since this did not eliminate the concern about meals and beverages that were more lavish than necessary, however, Treasury Secretary Dillon explained that the exception would likely be accompanied by

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[168] Id.
[169] Id.
[170] Hearings on President Kennedy's Special Message, supra note xx, at 74.
[171] Id. Transportation was also deductible with respect to such business trips.
[172] Hearings on President Kennedy's Special Message, supra note xx, at 74.
[173] Id.

a proviso that the expenses not exceed a certain amount per day, which he pegged at the $4-$7 range.[174]

The response to Kennedy's vow to limit deductions for travel and entertainment expenses reflected just how deep-seated the expense account society had become. Opponents argued that the proposed limits on expense account deductibility would effectively decimate entire industries. The restaurant industry was particularly vocal about the effect on its members. In hearings related to the expense account issue, lawyer Thomas Power, representing the National Restaurant Association, testified that "business entertaining would be entirely eliminated under the Administration's proposals except in very limited cases."[175] According to Power, that is because such expenses would only be deductible if the meal was consumed during the business meeting. "A meal furnished to a customer for the principal purpose of facilitating good will," which Power suggested was the principal basis for most business meals in restaurants, "would not fit within these limitations even though they are reasonable, legitimate business expenses, and certainly are necessary for the proper conduct of America's business today."[176] The consequence of this, according to Power, is that "much of the food and beverage entertainment business would be eliminated because it would be incurred at a time obviously not conducive for the discussion of business. For example, the majority of the banquet business in the restaurant industry would be eliminated."[177] The National Restaurant Association estimated that "$800 million in wages and tips of 200,000 employees in the business would be threatened."[178]

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[174] Id.
[175] Hearings Before the Committee on Ways and Means, House of Representatives, 87th Cong., 1st Sess. on the Tax Recommendations of the President contained in his Message transmitted to Congress on April 21, 1961 at 1611 (1961) ("1961 House Hearings")
[176] 1961 House Hearings, supra note xx, at 1611
[177] 1961 House Hearings, supra note xx, at 1612.
[178] HELLERSTEIN, supra note xx, at 132.

New York restaurateur, Vincent Sardi, Jr., echoed and expanded on Power's prediction, stating that "we cannot exist in midtown Manhattan with people who just live in that area. We must bring in people to New York to support the hotel, the theaters, the restaurants, and all this business. If we eliminate or curtail extensively this business travel, we are wiping out this whole form of business throughout the entire country."[179] Representative John Byrnes of Wisconsin asked Sardi "what you are suggesting is that if the Treasury recommendations, as presented to us, are put into effect, midtown Manhattan would become a distressed area, and that they would have to seek relief through the legislation we just passed to retrain personnel" for different jobs elsewhere?[180] Sardi responded "that may sound like an exaggeration, Congressman, but it really isn't, and it isn't just midtown Manhattan," suggesting that midtown Chicago would be similarly affected.[181] According to Sardi, "the restaurant industry is in a state of recession right now not only in New York, but throughout the country. Part of it, of course, has been due to the scare of this expense account. There has been a drastic curtailment and a drastic holding back to see what is going to happen."[182]

Opponents argued that the proposed limits on expense account deductibility would effectively decimate the restaurant industry. The National Restaurant Association estimated that "over $2 billion a year is reported as business expenses for food and beverages."[183] These expenses were often concentrated in certain areas, making the effect of their demise all the more

[179] 1961 House Hearings, supra note xx, at 1617.
[180] 1961 House Hearings, supra note xx, at 1625.
[181] 1961 House Hearings, supra note xx, at 1625.
[182] 1961 House Hearings, supra note xx, at 1620.
[183] JEROME R. HELLERSTEIN, TAXES, LOOPHOLES & MORALS 132 (1963).

devastating. According to one estimate, in 1957 "some 80 per cent of luncheons served at top Manhattan restaurants like '21,' Le Pavilion and Chambord . . . are expensed."[184]

Members of the restaurant industry were not alone in predicting doom without expense account spending. John Lesure, a representative of the American Hotel Association, claimed that the proposed limits on expense accounts would devastate the hotel industry, especially given an anticipated decline in convention business. "In an industry in which the net income for 1960 was only 3.2 percent of its revenue, and that depends upon business travel for 60 percent of that revenue, a loss of as little as 5 percent of its business could be fatal."[185] Representative Milton Glenn, a Republican from New Jersey whose district included Atlantic City, underscored this point, testifying that "any curtailment of the use of an expense account will be disastrous to the economy of the New Jersey resort areas."[186]

Proponents of keeping the rules for deducting entertainment expenses largely intact protested the notion that it financed personal consumption. The National Restaurant Association's Thomas Power conceded that "these expenses afford some advantage of a personal nature," but argued that this personal advantage was "grossly exaggerated."[187] Power asserted that "it is not the advantage that the person who has never experienced an expense account would imagine it to be. . . The majority of men that must constantly travel or consistently entertain at the so-called plush cocktail parties, restaurants, social functions, etc., become very tired of this mode of living."[188]

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[184] Sanford Brown, *I'll Just Sign: Those Big-Figure Expense Accounts*, NEWSWEEK, May 20, 1957, at 87.
[185] 1961 House Hearings, supra note xx, at 1645.
[186] 1961 House Hearings, supra note xx, at 1649 (Statement of Rep. Milton Glenn (R-N.J.).
[187] 1961 House Hearings, supra note xx, at 1614.
[188] 1961 House Hearings, supra note xx, at 1614.

Although business representatives were careful to align themselves with those concerned about "abuse," they painted such abuses as outliers, distinct from what their customers and clients were doing. John Lesure prefaced his testimony on behalf of the hotel industry to the Ways and Means Committee by noting that "we do not in any way approve of the abuses that may have occurred in recent years when taxpayers have attempted to deduct as business expenses the cost of an African safari, or the maintenance of yachts or hunting lodges."[189] Nevertheless, Lesure "object[ed] strenuously to the establishment of arbitrary restrictions on legitimate business expenses," which presumably included hotel stays at his members' establishments.[190] Clarence Turner, an accountant speaking on behalf of the Council of State Chambers of Commerce, opined that "the abuse of expense accounts is confined to a relatively few persons."[191] "I have found" Turner recounted, "the vast majority of businessmen trying honestly and conscientiously to separate personal from business expense and report the latter accurately."[192]

Kennedy's plan found some support in Congress. For instance, Senator Paul Douglas, a Democrat from Illinois, called the deduction for expense accounts and entertainment "one of the grossest abuses in American business."[193] Nevertheless, the opponents of Kennedy's plan were ultimately successful in preserving most of the tax structure that supported the expense account society. As Jerome Hellerstein colorfully declared, the "proposals to restrict entertainment expenses were torn to shreds by Congress."[194] What came out of Capitol Hill," Hellerstein explained, "was in essence a reaffirmation of the rule that business-entertainment expenses are to

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[189] 1961 House Hearings, supra note xx, at 1643 (statement of John Lesure, American Hotel Association).
[190] 1961 House Hearings, supra note xx, at 1643 (statement of John Lesure, American Hotel Association).
[191] 1961 House Hearings, supra note xx, at 1661 (statement of Clarence L. Turner, Council of State Chambers of Commerce).
[192] Id.
[193] Legislative History of H.R. 10650, 87th Cong., The Revenue Act of 1962, , Pub. L. 87-834, 90th Cong., 1st Sess. 2942 (1967) (statement of Sen. Paul Douglas).
[194] JEROME R. HELLERSTEIN, TAXES, LOOPHOLES, & MORALS 135 (1963).

be allowed, plus some new standards for judging whether an expense is truly a business expense, and a tightening up of the records required to be kept to prove that the expenditures were actually made."[195] The travel and entertainment rules adopted in the 1962 Act may have been "the culmination of a long campaign by the Treasury Department to put an end to "expense account living,""[196] but they hardly fulfilled the campaign's mission.

Under the provisions enacted in 1962, entertainment had to be "directly related to the active conduct" of the taxpayer's trade or business or, if the entertainment directly preceded or followed "a substantial and bona fide business discussion," then the entertainment expense must be "associated with" the active conduct of the taxpayer's trade or business.[197] Although taxpayers had to show some business relationship to an entertainment expense even prior to 1962, the intention was that the amendment to the Code in 1962 would require that the taxpayer establish "a greater degree of proximate relation" than he had previously.[198] Congress intended that the deduction would be denied "where the possibility of the expenditure resulting in the production of income was remote," but this was hardly a high standard.[199]

That does not mean that observers thought the 1962 Act's reform provisions would have no effect. As Hellerstein explained, "the new law will undoubtedly curtail some of the worst abuses in extravagant living off the income-tax gravy train. The costs of African safaris and fishing cruises will now be difficult, if not impossible, to sustain for most taxpayers."[200] It also required

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[195] JEROME R. HELLERSTEIN, TAXES, LOOPHOLES, & MORALS 135 (1963).
[196] Dennis R. Powell, *Note, Effect of the 1962 Revenue Act on Travel, Entertainment, and Gift Deductions*, 38 NOTRE DAME LAW. 447, 447 (1963).
[197] Int. Rev. Code, § 274(a)(1)(A) (1954 Code).
[198] Daniel Candee Knickerbocker, Jr., *Entertainment and Related Deductions Under the Revenue Act of 1962*, 31 FORDHAM L. REV. 639, 642 (1963).
[199] Id. at 642.
[200] JEROME R. HELLERSTEIN, TAXES, LOOPHOLES AND MORALS 136 (1963).

more detailed record keeping to justify business expenses for meals and entertainment, which Hellerstein predicted "are likely to produce disallowances of unsubstantiated amounts of nondeductible expenditures that they have been getting away with for years."[201]

All of this led to "unprecedented" concern among businessmen and their advisers about the specific regulations as they were drafted to implement the 1962 Act's new rules.[202] Herbert Eagle, an insurance company executive, expressed concern that the documentation requirements would alter the "psyche of the go-get-'em salesman."[203] According to Eagle, "the substantiation requirement would tend to submerge the creative extrovert salesman in a deadening sea of detailed record keeping."[204] Hearings on these rules were moved to a larger hall and expanded from one to two days to accommodate the large number of witnesses seeking to testify in the hopes of softening the proposed regulations.[205] A total of fifty-one witnesses appeared on behalf of business interests during the hearings and the Ways and Means Committee and another two thousand wrote letters criticizing the regulations.[206] Businessmen formally resented what they considered to be an attempt "to penetrate further into the affairs that businessmen . . . feel is properly the business of business,"[207] but "there occasionally was an undercurrent of shocked realization that the good old days might really be gone after all."[208]

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[201] Hellerstein, supra note xx, at 137-138

[202] Robert Metz, *Businessmen Protest Changes in Expense-Account Tax Rules*, N.Y. TIMES, Dec. 3, 1962, at 49.

[203] Ronald J. Ostrow, *Area Executives Take Up Gauntlet Over Expense Account Deductions*, L.A. TIMES, Dec. 9, 1962, at K1, K3.

[204] Id.

[205] Metz, Businessmen Protest Changes, supra note xx, at 49.

[206] John D. Pomfret, *"Expense Account Living" Coming Under Close Scrutiny*, N.Y. TIMES, Dec. 10, 1962, at 13.

[207] Ronald J. Ostrow, *Area Executives Take Up Gauntlet Over Expense Account Deductions*, L.A. TIMES, Dec. 9, 1962, at K1.

[208] Pomfret, *Expense Account Living, supra* note xx, at 13.

Notwithstanding this concern, few thought the days of the expense account society were over. Many argued that the new restrictions "added nothing of any substance to the law" because much of the language that was used in the new provisions were similar to language that had been used by courts in enforcing the pre-existing law.[209] As long as taxpayers engaged in "shop talk" and kept appropriate records, they could continue to entertain as normal. As Hellerstein explained, "the standards are too vague and uncertain and will, I suspect, result in the continued allowance as deductible of too much of what is in truth personal living expense."[210]

The documentation rules also were more of an irritant than a real obstacle. Commissioner Mortimer Caplin, responding to complainers, explained that "many companies demand much greater detail from their employees" than what the documentation rules required.[211] Moreover, the truly dishonest taxpayers who exaggerated their expenses or made them up completely were just as likely to create fraudulent documentation as to forgo the activity altogether.[212] The prevailing sentiment seemed to be that if the law exceeded the commonly accepted view of what amount of tax avoidance was acceptable, it would simply be ignored. As one New York businessman warned, "if the government is determined to kill hunting lodges, pseudo business planes and phony business trips to Europe – that's great, but if they're going to start nickel

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[209] Knicerbocker, supra note xx, at 660.

[210] Hellerstein, supra note xx, at 138.

[211] Mortimer Caplin, *Letters to the Editor, Caplin and Congress*, WALL ST. J., Jan. 17, 1963, at 14.

[212] *See, e.g.*, Ostrow, *Area Executives Take up Gauntlet, supra* note xx, at K3 (quoting one businessmen who opined that "These requirements are going to produce some 'wonderful fiction.'"); *Expense Accounts: New Tax Rules Likely to Further Cut Abuses*, WALL ST. J., Oct. 11, 1962, at 1, 14 (noting that "a few cheaters . . . may have hit on a way to beat" the documentation requirement, such as one "Long Island executive who, by arrangement with his deliveryman, never pays the bill for daily deliveries of bread and cask to his house until it hits $100 or $150," which IRS agents had accepted in the past, "reasoning that if he paid $150 at one time for bakery goods he must have held a party.").

snatching, denying a business lunch and modest entertaining of clients, they'll be deceived, denied and defeated."[213]

It may be that the 1962 Act demonstrated the difficulty of legislating away what was already culturally embedded. As Michael Emmanuel and Norman Lipoff – two contemporary practitioners – explained "seldom has a new statute slashed so broadly across the practices and customs of the business community."[214] In effect, the statute was an attempt "for the first time to curb business practices which, over the span of a generation, had become a way of life."[215] Not surprisingly given this cultural entrenchment, the phrase "it's deductible" was not "vanishing from the American scene" in the aftermath of the 1962 Act as President Kennedy had hoped, although it was reportedly "no longer being uttered in such offhand fashion, nor quite so frequently, as it has been over the" previous two decades."[216] By 1964, Congress had already repealed an aspect of the travel and entertainment aspect of the new rules that had required allocation of transportation expenses between the time spent on a more than one week trip for business and personal reasons.[217] It was not long before columnists were once again advising individuals with "travel fever" about the myriad ways they could cultivate a business connection in their desired destination and document it appropriately both before and during the trip to ensure that much of it would be deductible.[218]

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[213] Robert Metz, *Businessmen Protest Changes in Expense-Account Tax Rules*, N.Y. TIMES, Dec. 3, 1962, at 49, 52.
[214] Michael G. Emmanuel and Norman H. Lipoff, *Travel and Entertainment: The New World of Section 274*, 18 TAX L. REV. 487 (1963).
[215] Emmanuel and Lipoff, supra note xx, at 487.
[216] Eileen Shanahan, *Expense Accounts: To Strict?* N.Y. TIMES, May 12, 1963, at E8. *See* Peter Bart, *Advertising: Entertainment is Less Lavish*, N.Y. TIMES, March 8, 1964, at F12 (noting that subtle changes were occurring in entertainment spending, although prompted by factors other than tax in many cases).
[217] William A. Klein, *The Deductibility of Transportation Expenses of a Combination Business and Pleasure Trip – a Conceptual Analysis*, 18 Stan. L. Rev. 1099, 1177 (1966).
[218] Robert McKay, *Combine Travel, Business for Tax Break*, CHI. TRIB., Feb. 18, 1968, at N6.