

this section, a taxpayer must treat all hours spent by a person on direct contact lobbying (as well as the hours that person spends in connection with direct contact lobbying, including time spent traveling that is allocable to the direct contact lobbying) as labor hours allocable to lobbying activities. An activity is direct contact lobbying if it is a meeting, telephone conversation, letter, or other similar means of communication with a legislator (other than a local legislator) or covered executive branch official (as defined in section 162(e)(6)) and otherwise qualifies as a lobbying activity. A person who engages in research, preparation, and other background activities related to direct contact lobbying but who does not make direct contact with a legislator or covered executive branch official is not engaged in direct contact lobbying.

(3) *Taxpayer defined.* For purposes of this section, a taxpayer includes a tax-exempt organization subject to section 6033(e).

(h) *Effective date.* This section is effective for amounts paid or incurred on or after July 21, 1995. Taxpayers must adopt a reasonable interpretation of sections 162(e)(1)(A) and (D) for amounts paid or incurred before this date.

[T.D. 8602, 60 FR 37573, July 21, 1995]

§ 1.162-29 Influencing legislation.

(a) *Scope.* This section provides rules for determining whether an activity is influencing legislation for purposes of section 162(e)(1)(A). This section does not apply for purposes of sections 4911 and 4945 and the regulations thereunder.

(b) *Definitions.* For purposes of this section—

(1) *Influencing legislation.* Influencing legislation means—

(i) Any attempt to influence any legislation through a lobbying communication; and

(ii) All activities, such as research, preparation, planning, and coordination, including deciding whether to make a lobbying communication, engaged in for a purpose of making or supporting a lobbying communication, even if not yet made. See paragraph (c) of this section for rules for determining

the purposes for engaging in an activity.

(2) *Attempt to influence legislation.* An attempt to influence any legislation through a lobbying communication is making the lobbying communication.

(3) *Lobbying communication.* A lobbying communication is any communication (other than any communication compelled by subpoena, or otherwise compelled by Federal or State law) with any member or employee of a legislative body or any other government official or employee who may participate in the formulation of the legislation that—

(i) Refers to specific legislation and reflects a view on that legislation; or

(ii) Clarifies, amplifies, modifies, or provides support for views reflected in a prior lobbying communication.

(4) *Legislation.* Legislation includes any action with respect to Acts, bills, resolutions, or other similar items by a legislative body. Legislation includes a proposed treaty required to be submitted by the President to the Senate for its advice and consent from the time the President's representative begins to negotiate its position with the prospective parties to the proposed treaty.

(5) *Specific legislation.* Specific legislation includes a specific legislative proposal that has not been introduced in a legislative body.

(6) *Legislative bodies.* Legislative bodies are Congress, state legislatures, and other similar governing bodies, excluding local councils (and similar governing bodies), and executive, judicial, or administrative bodies. For this purpose, administrative bodies include school boards, housing authorities, sewer and water districts, zoning boards, and other similar Federal, State, or local special purpose bodies, whether elective or appointive.

(7) *Examples.* The provisions of this paragraph (b) are illustrated by the following examples.

Example 1. Taxpayer P's employee, A, is assigned to approach members of Congress to gain their support for a pending bill. A drafts and P prints a position letter on the bill. P distributes the letter to members of Congress. Additionally, A personally contacts several members of Congress or their staffs to seek support for P's position on the bill.

The letter and the personal contacts are lobbying communications. Therefore, P is influencing legislation.

Example 2. Taxpayer R is invited to provide testimony at a congressional oversight hearing concerning the implementation of The Financial Institutions Reform, Recovery, and Enforcement Act of 1989. Specifically, the hearing concerns a proposed regulation increasing the threshold value of commercial and residential real estate transactions for which an appraisal by a state licensed or certified appraiser is required. In its testimony, R states that it is in favor of the proposed regulation. Because R does not refer to any specific legislation or reflect a view on any such legislation, R has not made a lobbying communication. Therefore, R is not influencing legislation.

Example 3. State X enacts a statute that requires the licensing of all day-care providers. Agency B in State X is charged with writing rules to implement the statute. After the enactment of the statute, Taxpayer S sends a letter to Agency B providing detailed proposed rules that S recommends Agency B adopt to implement the statute on licensing of day-care providers. Because the letter to Agency B neither refers to nor reflects a view on any specific legislation, it is not a lobbying communication. Therefore, S is not influencing legislation.

Example 4. Taxpayer T proposes to a State Park Authority that it purchase a particular tract of land for a new park. Even if T's proposal would necessarily require the State Park Authority eventually to seek appropriations to acquire the land and develop the new park, T has not made a lobbying communication because there has been no reference to, nor any view reflected on, any specific legislation. Therefore, T's proposal is not influencing legislation.

Example 5. (i) Taxpayer U prepares a paper that asserts that lack of new capital is hurting State X's economy. The paper indicates that State X residents either should invest more in local businesses or increase their savings so that funds will be available to others interested in making investments. U forwards a summary of the unpublished paper to legislators in State X with a cover letter that states in part:

You must take action to improve the availability of new capital in the state.

(ii) Because neither the summary nor the cover letter refers to any specific legislative proposal and no other facts or circumstances indicate that they refer to an existing legislative proposal, forwarding the summary to legislators in State X is not a lobbying communication. Therefore, U is not influencing legislation.

(iii) Q, a member of the legislature of State X, calls U to request a copy of the unpublished paper from which the summary was prepared. U forwards the paper with a cover

letter that simply refers to the enclosed materials. Because U's letter to Q and the unpublished paper do not refer to any specific legislation or reflect a view on any such legislation, the letter is not a lobbying communication. Therefore, U is not influencing legislation.

Example 6. (i) Taxpayer V prepares a paper that asserts that lack of new capital is hurting the national economy. The paper indicates that lowering the capital gains rate would increase the availability of capital and increase tax receipts from the capital gains tax. V forwards the paper to its representatives in Congress with a cover letter that says, in part:

I urge you to support a reduction in the capital gains tax rate.

(ii) V's communication is a lobbying communication because it refers to and reflects a view on a specific legislative proposal (*i.e.*, lowering the capital gains rate). Therefore, V is influencing legislation.

Example 7. Taxpayer W, based in State A, notes in a letter to a legislator of State A that State X has passed a bill that accomplishes a stated purpose and then says that State A should pass such a bill. No such bill has been introduced into the State A legislature. The communication is a lobbying communication because it refers to and reflects a view on a specific legislative proposal. Therefore, W is influencing legislation.

Example 8. (i) Taxpayer Y represents citrus fruit growers. Y writes a letter to a United States senator discussing how pesticide O has benefited citrus fruit growers and disputing problems linked to its use. The letter discusses a bill pending in Congress and states in part:

This bill would prohibit the use of pesticide O. If citrus growers are unable to use this pesticide, their crop yields will be severely reduced, leading to higher prices for consumers and lower profits, even bankruptcy, for growers.

(ii) Y's views on the bill are reflected in this statement. Thus, the communication is a lobbying communication, and Y is influencing legislation.

Example 9. (i) B, the president of Taxpayer Z, an insurance company, meets with Q, who chairs the X state legislature's committee with jurisdiction over laws regulating insurance companies, to discuss the possibility of legislation to address current problems with surplus-line companies. B recommends that legislation be introduced that would create minimum capital and surplus requirements for surplus-line companies and create clearer guidelines concerning the risks that surplus-line companies can insure. B's discussion with Q is a lobbying communication because B refers to and reflects a view on a specific legislative proposal. Therefore, Z is influencing legislation.

(ii) Q is not convinced that the market for surplus-line companies is substantial enough to warrant such legislation and requests that B provide information on the amount and types of risks covered by surplus-line companies. After the meeting, B has employees of Z prepare estimates of the percentage of property and casualty insurance risks handled by surplus-line companies. B sends the estimates with a cover letter that simply refers to the enclosed materials. Although B's follow-up letter to Q does not refer to specific legislation or reflect a view on such legislation, B's letter supports the views reflected in the earlier communication. Therefore, the letter is a lobbying communication and Z is influencing legislation.

(c) *Purpose for engaging in an activity*—(1) *In general.* The purposes for engaging in an activity are determined based on all the facts and circumstances. Facts and circumstances include, but are not limited to—

(i) Whether the activity and the lobbying communication are proximate in time;

(ii) Whether the activity and the lobbying communication relate to similar subject matter;

(iii) Whether the activity is performed at the request of, under the direction of, or on behalf of a person making the lobbying communication;

(iv) Whether the results of the activity are also used for a nonlobbying purpose; and

(v) Whether, at the time the taxpayer engages in the activity, there is specific legislation to which the activity relates.

(2) *Multiple purposes.* If a taxpayer engages in an activity both for the purpose of making or supporting a lobbying communication and for some nonlobbying purpose, the taxpayer must treat the activity as engaged in partially for a lobbying purpose and partially for a nonlobbying purpose. This division of the activity must result in a reasonable allocation of costs to influencing legislation. See § 1.162-28 (allocation rules for certain expenditures to which section 162(e)(1) applies). A taxpayer's treatment of these multiple-purpose activities will, in general, not result in a reasonable allocation if it allocates to influencing legislation—

(i) Only the incremental amount of costs that would not have been incurred but for the lobbying purpose; or

(ii) An amount based solely on the number of purposes for engaging in that activity without regard to the relative importance of those purposes.

(3) *Activities treated as having no purpose to influence legislation.* A taxpayer that engages in any of the following activities is treated as having done so without a purpose of making or supporting a lobbying communication—

(i) Before evidencing a purpose to influence any specific legislation referred to in paragraph (c)(3)(i)(A) or (B) of this section (or similar legislation)—

(A) Determining the existence or procedural status of specific legislation, or the time, place, and subject of any hearing to be held by a legislative body with respect to specific legislation; or

(B) Preparing routine, brief summaries of the provisions of specific legislation;

(ii) Performing an activity for purposes of complying with the requirements of any law (for example, satisfying state or federal securities law filing requirements);

(iii) Reading any publications available to the general public or viewing or listening to other mass media communications; and

(iv) Merely attending a widely attended speech.

(4) *Examples.* The provisions of this paragraph (c) are illustrated by the following examples.

Example 1. (i) *Facts.* In 1997, Agency F issues proposed regulations relating to the business of Taxpayer W. There is no specific legislation during 1997 that is similar to the regulatory proposal. W undertakes a study of the impact of the proposed regulations on its business. W incorporates the results of that study in comments sent to Agency F in 1997. In 1998, legislation is introduced in Congress that is similar to the regulatory proposal. Also in 1998, W writes a letter to Senator P stating that it opposes the proposed legislation. W encloses with the letter a copy of the comments it sent to Agency F.

(ii) *Analysis.* W's letter to Senator P refers to and reflects a view on specific legislation and therefore is a lobbying communication. Although W's study of the impact of the proposed regulations is proximate in time and similar in subject matter to its lobbying communication, W performed the study and incorporated the results in comments sent to Agency F when no legislation with a similar subject matter was pending (a nonlobbying use). On these facts, W engaged in the study solely for a nonlobbying purpose.

Example 2. (i) *Facts.* The governor of State Q proposes a budget that includes a proposed sales tax on electricity. Using its records of electricity consumption, Taxpayer Y estimates the additional costs that the budget proposal would impose upon its business. In the same year, Y writes to members of the state legislature and explains that it opposes the proposed sales tax. In its letter, Y includes its estimate of the costs that the sales tax would impose on its business. Y does not demonstrate any other use of its estimates.

(ii) *Analysis.* The letter is a lobbying communication (because it refers to and reflects a view on specific legislation, the governor's proposed budget). Y's estimate of additional costs under the proposal supports the lobbying communication, is proximate in time and similar in subject matter to a specific legislative proposal then in existence, and is not used for a nonlobbying purpose. Based on these facts, Y estimated its additional costs under the budget proposal solely to support the lobbying communication.

Example 3. (i) *Facts.* A senator in the State Q legislature announces her intention to introduce legislation to require health insurers to cover a particular medical procedure in all policies sold in the state. Taxpayer Y has different policies for two groups of employees, one of which covers the procedure and one of which does not. After the bill is introduced, Y's legislative affairs staff asks Y's human resources staff to estimate the additional cost to cover the procedure for both groups of employees. Y's human resources staff prepares a study estimating Y's increased costs and forwards it to the legislative affairs staff. Y's legislative staff then writes to members of the state legislature and explains that it opposes the proposed change in insurance coverage based on the study. Y's legislative affairs staff thereafter forwards the study, prepared for its use in opposing the statutory proposal, to its labor relations staff for use in negotiations with employees scheduled to begin later in the year.

(ii) *Analysis.* The letter to legislators is a lobbying communication (because it refers to and reflects a view on specific legislation). The activity of estimating Y's additional costs under the proposed legislation relates to the same subject as the lobbying communication, occurs close in time to the lobbying communication, is conducted at the request of a person making a lobbying communication, and relates to specific legislation then in existence. Although Y used the study in its labor negotiations, mere use for that purpose does not establish that Y estimated its additional costs under the proposed legislation in part for a nonlobbying purpose. Thus, based on all the facts and circumstances, Y estimated the additional costs it would incur under the proposal solely

to make or support the lobbying communication.

Example 4. (i) *Facts.* After several years of developmental work under various contracts, in 1996, Taxpayer A contracts with the Department of Defense (DOD) to produce a prototype of a new generation military aircraft. A is aware that DOD will be able to fund the contract only if Congress appropriates an amount for that purpose in the upcoming appropriations process. In 1997, A conducts simulation tests of the aircraft and revises the specifications of the aircraft's expected performance capabilities, as required under the contract. A submits the results of the tests and the revised specifications to DOD. In 1998, Congress considers legislation to appropriate funds for the contract. In that connection, A summarizes the results of the simulation tests and of the aircraft's expected performance capabilities, and submits the summary to interested members of Congress with a cover letter that encourages them to support appropriations of funds for the contract.

(ii) *Analysis.* The letter is a lobbying communication (because it refers to specific legislation (*i.e.*, appropriations) and requests passage). The described activities in 1996, 1997, and 1998 relate to the same subject as the lobbying communication. The summary was prepared specifically for, and close in time to, that communication. Based on these facts, the summary was prepared solely for a lobbying purpose. In contrast, A conducted the tests and revised the specifications to comply with its production contract with DOD. A conducted the tests and revised the specifications solely for a nonlobbying purpose.

Example 5. (i) *Facts.* C, president of Taxpayer W, travels to the state capital to attend a two-day conference on new manufacturing processes. C plans to spend a third day in the capital meeting with state legislators to explain why W opposes a pending bill unrelated to the subject of the conference. At the meetings with the legislators, C makes lobbying communications by referring to and reflecting a view on the pending bill.

(ii) *Analysis.* C's traveling expenses (transportation and meals and lodging) are partially for the purpose of making or supporting the lobbying communications and partially for a nonlobbying purpose. As a result, under paragraph (c)(2) of this section, W must reasonably allocate C's traveling expenses between these two purposes. Allocating to influencing legislation only C's incremental transportation expenses (*i.e.*, the taxi fare to meet with the state legislators) does not result in a reasonable allocation of traveling expenses.

Example 6. (i) *Facts.* On February 1, 1997, a bill is introduced in Congress that would affect Company E. Employees in E's legislative

affairs department, as is customary, prepare a brief summary of the bill and periodically confirm the procedural status of the bill through conversations with employees and members of Congress. On March 31, 1997, the head of E's legislative affairs department meets with E's President to request that B, a chemist, temporarily help the legislative affairs department analyze the bill. The President agrees, and suggests that B also be assigned to draft a position letter in opposition to the bill. Employees of the legislative affairs department continue to confirm periodically the procedural status of the bill. On October 31, 1997, B's position letter in opposition to the bill is delivered to members of Congress.

(ii) *Analysis.* B's letter is a lobbying communication because it refers to and reflects a view on specific legislation. Under paragraph (c)(3)(i) of this section, the assignment of B to assist the legislative affairs department in analyzing the bill and in drafting a position letter in opposition to the bill evidences a purpose to influence legislation. Neither the activity of periodically confirming the procedural status of the bill nor the activity of preparing the routine, brief summary of the bill before March 31 constitutes influencing legislation. In contrast, periodically confirming the procedural status of the bill on or after March 31 relates to the same subject as, and is close in time to, the lobbying communication and is used for no nonlobbying purpose. Consequently, after March 31, E determined the procedural status of the bill for the purpose of supporting the lobbying communication by B.

(d) *Lobbying communication made by another.* If a taxpayer engages in activities for a purpose of supporting a lobbying communication to be made by another person (or by a group of persons), the taxpayer's activities are treated under paragraph (b) of this section as influencing legislation. For example, if a taxpayer or an employee of the taxpayer (as a volunteer or otherwise) engages in an activity to assist a trade association in preparing its lobbying communication, the taxpayer's activities are influencing legislation even if the lobbying communication is made by the trade association and not the taxpayer. If, however, the taxpayer's employee, acting outside the employee's scope of employment, volunteers to engage in those activities, then the taxpayer is not influencing legislation.

(e) *No lobbying communication.* Paragraph (e) of this section applies if a taxpayer engages in an activity for a

purpose of making or supporting a lobbying communication, but no lobbying communication that the activity supports has yet been made.

(1) *Before the filing date.* Under this paragraph (e)(1), if on the filing date of the return for any taxable year the taxpayer no longer expects, under any reasonably foreseeable circumstances, that a lobbying communication will be made that is supported by the activity, then the taxpayer will be treated as if it did not engage in the activity for a purpose of making or supporting a lobbying communication. Thus, the taxpayer need not treat any amount allocated to that activity for that year under § 1.162-28 as an amount to which section 162(e)(1)(A) applies. The filing date for purposes of paragraph (e) of this section is the earlier of the time the taxpayer files its timely return for the year or the due date of the timely return.

(2) *After the filing date—(i) In general.* If, at any time after the filing date, the taxpayer no longer expects, under any reasonably foreseeable circumstances, that a lobbying communication will be made that is supported by the activity, then any amount previously allocated under § 1.162-28 to the activity and disallowed under section 162(e)(1)(A) is treated as an amount that is not subject to section 162(e)(1)(A) and that is paid or incurred only at the time the taxpayer no longer expects that a lobbying communication will be made.

(ii) *Special rule for certain tax-exempt organizations.* For a tax-exempt organization subject to section 6033(e), the amounts described in paragraph (e)(2)(i) of this section are treated as reducing (but not below zero) its expenditures to which section 162(e)(1) applies beginning with that year and continuing for subsequent years to the extent not treated in prior years as reducing those expenditures.

(f) *Anti-avoidance rule.* If a taxpayer, alone or with others, structures its activities with a principal purpose of achieving results that are unreasonable in light of the purposes of section 162(e)(1)(A) and section 6033(e), the

Commissioner can recast the taxpayer's activities for federal tax purposes as appropriate to achieve tax results that are consistent with the intent of section 162(e)(1)(A), section 6033(e) (if applicable), and this section, and the pertinent facts and circumstances.

(g) *Taxpayer defined.* For purposes of this section, a taxpayer includes a tax-exempt organization subject to section 6033(e).

(h) *Effective date.* This section is effective for amounts paid or incurred on or after July 21, 1995. Taxpayers must adopt a reasonable interpretation of section 162(e)(1)(A) for amounts paid or incurred before this date.

[T.D. 8602, 60 FR 37575, July 21, 1995]

§ 1.162(k)-1 Disallowance of deduction for reacquisition payments.

(a) *In general.* Except as provided in paragraph (b) of this section, no deduction otherwise allowable is allowed under Chapter 1 of the Internal Revenue Code for any amount paid or incurred by a corporation in connection with the reacquisition of its stock or the stock of any related person (as defined in section 465(b)(3)(C)). Amounts paid or incurred in connection with the reacquisition of stock include amounts paid by a corporation to reacquire its stock from an ESOP that are used in a manner described in section 404(k)(2)(A). See § 1.404(k)-3.

(b) *Exceptions.* Paragraph (a) of this section does not apply to any—

(1) Deduction allowable under section 163 (relating to interest);

(2) Deduction for amounts that are properly allocable to indebtedness and amortized over the term of such indebtedness;

(3) Deduction for dividends paid (within the meaning of section 561); or

(4) Amount paid or incurred in connection with the redemption of any stock in a regulated investment company that issues only stock which is redeemable upon the demand of the shareholder.

(c) *Effective date.* This section applies with respect to amounts paid or incurred on or after August 30, 2006.

[T.D. 9282, 71 FR 51473, Aug. 30, 2006]

§ 1.163-1 Interest deduction in general.

(a) Except as otherwise provided in sections 264 to 267, inclusive, interest paid or accrued within the taxable year on indebtedness shall be allowed as a deduction in computing taxable income. For rules relating to interest on certain deferred payments, see section 483 and the regulations thereunder.

(b) Interest paid by the taxpayer on a mortgage upon real estate of which he is the legal or equitable owner, even though the taxpayer is not directly liable upon the bond or note secured by such mortgage, may be deducted as interest on his indebtedness. Pursuant to the provisions of section 163(c), any annual or periodic rental payment made by a taxpayer on or after January 1, 1962, under a redeemable ground rent, as defined in section 1055(c) and paragraph (b) of § 1.1055-1, is required to be treated as interest on an indebtedness secured by a mortgage and, accordingly, may be deducted by the taxpayer as interest on his indebtedness. Section 163(c) has no application in respect of any annual or periodic rental payment made prior to January 1, 1962, or pursuant to an arrangement which does not constitute a "redeemable ground rent" as defined in section 1055(c) and paragraph (b) of § 1.1055-1. Accordingly, annual or periodic payments of Pennsylvania ground rents made before, on, or after January 1, 1962, are deductible as interest if the ground rent is redeemable. An annual or periodic rental payment under a Maryland redeemable ground rent made prior to January 1, 1962, is deductible in accordance with the rules and regulations applicable at the time such payment was made. Any annual or periodic rental payment under a Maryland redeemable ground rent made by the taxpayer on or after January 1, 1962, is, pursuant to the provisions of section 163(c), treated as interest on an indebtedness secured by a mortgage and, accordingly, is deductible by the taxpayer as interest on his indebtedness. In any case where the ground rent is irredeemable, any annual or periodic ground rent payment shall be treated as rent and shall be deductible only to the extent that the payment constitutes a proper business expense. Amounts paid in redemption of a ground rent shall not be treated as