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Halsey & Peloubet: Federal Taxation and Unreasonable Compensation

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positive of the issue; they are not conclusive nor do they purport to be. But they serve, at least, to underscore the speculative nature of any conclusions that would emphasize the impact of intemperate statements on the voters.[6]

For this reason, Professor Gitelman has been careful to caution against excessive or inflammatory communications to employees in an effort to dissuade them from supporting a union. This emphasis is highly desirable since the Board has become concerned of late with inflammatory communications concerning such matters as race and violent strikes,[7] and the courts, and, to a lesser extent, the Board, have undertaken the condemnation of major misrepresentations or misstatements of fact in election campaigns.[8]

On the other hand, in *Appendix A, Employer Notices, Letters and Speeches*, the author presents a number of examples of material which employers have used during election campaigns. These items are prefaced with the caveat that the author does not endorse or recommend them but merely presents them as examples of what some employers have used. However, the first item, a bulletin board notice, has figured in a number of Board decisions and has been held to contain an implied threat to employees in violation of section 8(a)(1) of the act.[9] The other material, a letter to employees and several employer speeches, appears to be a bit more extreme than the author counselled in his text, and one of the speeches reproduced from the *Lux Clock Mfg. Co.* case[10] is of dubious innocence today.

Subject to these qualifications, the study represents a careful, painstaking effort to present a subject, complicated from both an emotional and a legal standpoint, clearly and concisely in layman's language. In this the author has been successful, and the volume should be of real usefulness to the audience to which it is directed.

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Federal Taxation and Unreasonable Compensation. By Crawford C. Halsey & Maurice E. Peloubet: Ronald Press, New York, 1964, pp. 180.

Perhaps one valid generalization about our legal process is that the legislatively-imposed standard of "reasonableness" has left the judicial system with difficult problems of interpretation. A perfect case in point is the provision of Section 162(a) of the 1954 Internal Revenue Code, as amended, which permits corporations an income tax deduction for

6 Bok, supra note 3, at 72-73.

7 General Indus. Electronics Co., 146 N.L.R.B. No. 115 (April 28, 1964); Patz Co., 4 CCH Lab. L. Rep. ¶ 12958 (1964).

8 See, e.g., NLRB v. Gilmore Indus., Inc., 341 F.2d 240 (6th Cir. 1965); NLRB v. Bonnie Enterprises, Inc., 341 F.2d 712 (4th Cir. 1965).

9 M. Lowenstein & Sons, Inc., 150 N.L.R.B. No. 66 (1964); White Oaks Acres, Inc., 134 N.L.R.B. 1145 (1961).

10 113 N.L.R.B. 1194 (1955).

> a *reasonable* allowance for salaries or other compensation for personal services actually rendered. (Emphasis added.)

A rapid examination of the legislative history of this provision reveals, surprisingly, that the 1965 version is precisely the same as its counterpart in the 1918 Revenue Act, which was the very first federal law to allow for a deduction of this nature. That times have indeed changed since 1918 is obvious to everyone, but it can be briefly and amusingly illustrated by a moment of reflection upon the words of then United States Congressman Henry T. Rainey of Illinois, who, in the course of delivering the final speech to the United States House of Representatives immediately preceding its vote on the bill which became the 1918 Revenue Act, spoke as follows:

> I propose hereafter to advocate individual income taxes to the very best of my ability, an income-tax system which contemplates taking the taxes entirely off industrial organizations and off all the instruments used for the transaction of business, a system which will preserve intact the business of the country and which will reach the incomes of individuals only. There are easy methods by which we can compel corporations to distribute, when they do not properly distribute, earnings, and when the money reaches the bank accounts of individuals the Government can then reach out and take any amount of it that may be necessary, without interfering with business and without interfering with the wages of labor.[1]

Congressman Rainey's promised advocacy subsequent to the passage of this bill (which, incidentally, was assisted by his own vote of "Yea"[2]) was obviously not persuasive enough. Corporation income taxes are still with us and, indeed, it would be safe to predict that they will persist for at least the near future. Consequently, the original language respecting the corporation deduction for *reasonable* compensation payments remains very important. Its importance is due to the negative pregnant implicit in the language of the provision, *to wit*: that *unreasonable* compensation payments are disallowed as a corporate deduction.

One could easily spend hours trying to prove the elusiveness of the so-called "reasonable man." Similarly, one could argue on end, and with considerable merit, that the use of the term "reasonable" in a taxing statute has cost society more than it has produced in revenue. Nonetheless, it exists as an important standard in the administration of the tax laws and must therefore be treated purposefully.

One such treatment is that of Messrs. Crawford C. Halsey and Maurice E. Peloubet, who together have authored a concise and valuable handbook for the corporate tax practitioner. Both of the authors are certified public accountants and partners in the internationally-known accounting firm of Price Waterhouse & Co. The purpose of the book is stated to be to consider the following problem: when may compensation of a corporate employee be found *unreasonable* and therefore not deductible under section 162(a).

1 57 Cong. Rec. 3034 (1919).
2 Id. at 3035.

The book succeeds in this purpose. To the tax scholar, its chief merit will be the exhaustive compilation of court decisions on this precise subject; to the practitioner it will be valuable for its practical suggestions of how to avoid problems with the courts and with the Internal Revenue Service while still allowing corporations to deduct meaningful compensation payments. To the student who aspires to perform professional tax counselling services, the book is helpful for its analysis of all of the recurrent factors determining reasonableness which appear in the judicial decisions.

The authors accurately point out that the problem is perhaps greatest in the context of the smaller, closely-held corporation, rather than in the huge publicly-held company where excessiveness or unreasonableness of any sort can be eliminated through the device of a stockholder's derivative suit. This is borne out by the cases listed and analyzed briefly in the book. The case names are overwhelmingly those of publicly-unknown or local corporations rather than the typical industrial giant concerns. This is not to suggest that what might well amount to "unreasonableness" by some standards does not exist in the larger companies; on the contrary, the authors point out as an example that Mr. Eugene Grace, then chairman of the board, Bethlehem Steel Corporation, received in salary and bonus in 1956 something in excess of $800,000. They then add parenthetically the interesting statistic that at the same time, Mr. Roger M. Blough, chairman of the board of the much larger United States Steel Corporation, received only approximately $265,000 from the same sources.

Because most of us are unlikely to be in the position of advising either Mr. Grace or Mr. Blough, or their companies, the particular problem of what is reasonable compensation for the head of a major steel company is strictly academic. But for many of us, the broader problem is not only very real but frequently encountered. For the authors' suggestions on steps to be taken in order to avoid the problem in the first place, as well as to assist in easing its impact when it is in fact encountered, the tax bar should be grateful.

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