Office of Chief Counsel
Internal Revenue Service
memorandum

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subject: **Request for Advice on Section 44, Disabled Access Credit**

This memorandum responds to your request for assistance dated December 19, 2003. This advice may not be used or cited as precedent.

ISSUES

(1) Whether any part of the purchase price (cash payments, bartered services, or promissory notes) of Programs 1, 2, or 3 qualifies as an ordinary and necessary business expense under section 162 of the Internal Revenue Code (the Code).

(2) Whether a taxpayer must be engaged in a trade or business to claim the disabled access credit under section 44 of the Code.

(3) Whether an eligible small business already in compliance with the ADA may claim a disabled access credit under section 44 for expenditures paid or incurred for the purchase of an upgraded or improved auxiliary aid or service.

(4) Whether an eligible small business may claim a disabled access credit under section 44 for expenditures paid or incurred for the purchase of an auxiliary aid or service which the business' disabled customers or clients do not use.

(5) Whether an eligible small business may claim each taxable year for multiple taxable years a disabled access credit under section 44 for expenditures paid or incurred in purchasing annual subscriptions to Programs 1 or 2.

(6) Whether an eligible small business must have a physical structure into which the public enters in order to meet the “place of public accommodation” requirement in the ADA.

(7) Whether amounts paid or incurred by an eligible small business to purchase Programs 1, 2, or 3 meet the definition of “eligible access expenditures” under section 44(c).

CONCLUSIONS

(1) Whether any part of the purchase price (cash payments, bartered services, or promissory notes) of Programs 1, 2, or 3 qualifies as an ordinary and necessary business expense under section 162 depends on the facts and circumstances of the particular taxpayer.

(2) A taxpayer must be engaged in a trade or business to claim the disabled access credit under section 44(a).

(3) Based on the plain language of section 44(c)(1), an eligible small business already in compliance with the ADA generally may not claim a disabled access credit for expenditures paid or incurred for the purchase of an upgraded or improved auxiliary aid or service because the expenditures are not paid or incurred to enable the eligible small business to comply with the applicable requirements of the ADA.

(4) An eligible small business may not claim the disabled access credit under section 44 for expenditures paid or incurred for the purchase of an auxiliary aid or service if under the business’ facts and circumstances the expenditures were not reasonable and necessary to accomplish a purpose described in section 44(c)(2).

(5) An eligible small business may not claim each taxable year for multiple taxable years a disabled access credit under section 44 for expenditures paid or incurred for annual subscriptions to Programs 1 or 2 because such annual subscription costs constitute an attempt to circumvent the limitation imposed by section 44(c)(1) and are unreasonable and unnecessary to accomplish the purpose of providing an effective method of making aurally delivered materials available to individuals with hearing impairments.

(6) Based on existing case law, it appears that an eligible small business must have a physical structure into which the public enters in order to meet the “place of public accommodation” requirement in the ADA.

(7) Amounts paid or incurred by an eligible small business to purchase Programs 1, 2, or 3 do not meet the definition of “eligible access expenditures” under section 44(c) if the expenditures were not paid or incurred to enable the eligible small business to comply with applicable requirements under the ADA.

FACTS

SCENARIO 1

Business 1 developed software that allowed hearing-impaired and speech-impaired individuals to communicate with a business (Program 1). Hearing-impaired and speech-impaired individuals could also use the software Business 1 described Program 1 as a . Business 1 represented that Program 1 rendered a participating business more accessible to disabled individuals, thereby qualifying the business for the disabled access credit under section 44.

Business 1 sold Program 1 for an annual subscription cost of $. Purchasers paid $ in cash and entered into a Agreement with a company affiliated with Business 1 to “earn” the $ balance of the purchase price by providing one or more services. These services most often consisted of . Purchasers of Program 1 were listed in by Business 1.

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Purchaser 1 operated a business that sold goods solely via the Internet. Purchaser 2 operated a business that sold goods and/or services at a physical place of business. Purchaser 3 had a physical place of business offering services off-site to the public.

The company affiliated with Business 1 sent to each purchaser a Form 1099 listing barter income of $ for services performed under the Agreement, and Business 1 instructed each purchaser to include the $ in income for the services performed, to claim a $ disabled access credit under section 44, and to deduct the excess of the purchase price, or $, as a business expense.

SCENARIO 2

Business 2 developed a software program (Program 2) and provided through which visually-impaired individuals could

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. Business 2 represented that Program 2 rendered a subscribing business more accessible to visually impaired individuals, thereby qualifying the business for the disabled access credit under section 44.

Business 2 sold Program 2 for an annual subscription cost of $. Purchasers of the annual subscription paid $ in cash and entered into a contract with an affiliate of Business 2 to “earn” the $ balance of the purchase price by bartering certain services. These services consisted of

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Purchaser 1 sold services (performed off-site) to the public from Purchaser 1’s private residence via the telephone. Purchaser 2 sold goods and/or services to the public at a physical place of business. Business 2’s affiliate sent to each purchaser a Form 1099 for the barter income. Program 2 promotional materials instructed the purchaser to include $ in income for the services, to claim a $ disabled access credit under section 44, and to deduct the excess of the purchase price, or $, as a business expense.

<u>SCENARIO 3</u>

Business 3 developed and sold Internet websites

Business 3 sold each URL/website for $. The purchaser satisfied its obligation to Business 3

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Concurrently, the purchaser contracted with an affiliate of Business 3 to make it accessible to the disabled. The affiliate sold the services for $. The purchaser paid $ of the $ in cash and signed a promissory note for the remaining $. Promotional materials indicate that

. The purchaser is told that he can

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The purchaser also

. The purchaser can

. Finally, the promissory note provides that

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Business 3 advised the purchaser that the

, that the purchaser would be entitled to a disabled access credit under section 44, and that personal expenses with respect to the

Based on the $ total cost, the purchaser claimed a $ disabled access credit under section 44 and a $ business expense deduction. This overall transaction is described as Program 3 for purposes of this memorandum.

LAW AND ANALYSIS

ISSUE 1

Section 162 allows a deduction for all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business, except items which are used as the basis for a deduction or a credit under provisions of law other than section 162. *See* § 1.162-1(a) of the Income Tax Regulations. Business expenses include advertising and other selling expenses. Section 1.162-1(a). However, the expenditure must also (1) be paid or incurred during the taxable year, (2) be for carrying on any trade or business, (3) be an “expense,” (4) be a “necessary” expense, and (5) be an “ordinary” expense. *See Commissioner v. Lincoln Sav. & Loan Assoc.*, 403 U.S. 345, 352 (1971). In addition, the expenditures must be substantiated.

Whether the Taxpayer is Carrying on a Trade or Business

First, the taxpayer must be “carrying on” a trade or business, in contrast to “starting up” a trade or business. Start-up expenditures cannot be currently deducted although, at the election of the taxpayer, they may be treated as deferred expenses that are allowed as a deduction prorated equally over a period of not less than 60 months. *See* § 195(a). Section 195(c)(1) defines “start-up expenditures,” in part, as any amount (A) paid or incurred in connection with investigating the creation or acquisition of an active trade or business, and (B) which, if paid or incurred in connection with the operation of an existing active trade or business (in the same field as the trade or business referred to in subparagraph (A)), would be allowable as a deduction for the taxable year in which paid or incurred. Thus, the taxpayer may amortize start-up expenditures even if the taxpayer is not “carrying on” a trade or business. However, the amortization election does not apply to amounts paid or incurred as part of the acquisition cost of a trade or business. *See* § 1.263(a)-5.

In addition, the taxpayer must be engaged in a "trade or business." Neither the Code nor the regulations contains a definition of "trade or business." Whether a taxpayer is engaged in a trade or business generally requires an examination of all the facts and circumstances. *Groetzinger v. Commissioner*, 480 U.S. 23, 36 (1987) (quoting *Higgins v. Commissioner*, 312 U.S. 212, 217 (1940)). In *Groetzinger*, the Supreme Court stated, "we accept the fact that to be engaged in a trade or business, the taxpayer must be involved in the activity with continuity and regularity and that the taxpayer's primary purpose for engaging in the activity must be for income or profit. A sporadic activity, a hobby, or an amusement diversion does not qualify." *Id.* at 35. Thus, the Court noted the importance of the scope of the activity (continuity and regularity) as well as the taxpayer's profit motive in establishing that the taxpayer is carrying on a trade or business. Some of the relevant factors to be considered in determining whether an activity is engaged in for profit are listed in section 1.183-2(b).[1]

Further, a taxpayer must show that its activities were undertaken with the "actual and honest" objective of making a profit. *Ferrell v. Commissioner*, 90 T.C. 1154 (1988) (quoting *Dreicer v. Commissioner*, 78 T.C. 642, 645 (1982), *aff'd without opinion* 702 F.2d 1205 (D.C. Cir. 1983)). "Profit" in this context means economic profit, independent of tax savings. *Id.* at 1181-1182 (quoting *Beck v. Commissioner*, 85 T.C. 557, 570 (1985) and *Surloff v. Commissioner*, 81 T.C. 210, 233 (1983)). *See also Herrick v. Commissioner*, 85 T.C. 237 (1985). Thus, for the taxpayers at issue in this memo to deduct the cost of the programs as a trade or business expense under section 162, they must show under their facts and circumstances that they are engaged in a regular and continuous activity, with a profit motive independent of any tax savings.

If a taxpayer is precluded from taking a deduction under section 162 because it does not engage in a trade or business, the taxpayer nonetheless may be able to deduct certain expenditures under section 212, which allows a deduction for ordinary and necessary expenses paid or incurred by an individual during the taxable year for the production or collection of income. Partnerships and corporations cannot deduct expenses under section 212, nor can any taxpayer that is carrying on a trade or business (in which case expenditures, if deductible, are deductible under section 162). Under section 212, an expense may be deducted by an individual if (1) it is paid or incurred during the taxable year; and (2) it is an ordinary and necessary expense for any of the following purposes: (a) for the production or collection of income which, if

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[1] Section 1.183-2(b) provides, in part, that the following factors should normally be taken into account: (1) the manner in which the taxpayer carries on the activity; (2) the expertise of the taxpayer or his advisors; (3) the time and effort expended by the taxpayer in carrying on the activity; (4) the expectation that assets used in the activity may appreciate in value; (5) the success of the taxpayer in carrying on other similar or dissimilar activities; (6) the taxpayer's history of income or losses with respect to the activity; (7) the amount of occasional profits, if any, which are earned; (8) the financial status of the taxpayer; (9) elements of personal pleasure or recreation.

and when realized, will be required to be included in income, (b) for the management, conservation, or maintenance of property held for the production of such income, or (c) in connection with the determination, collection, or refund of any tax. Section 1.212-1(a). Thus, unlike the requirements for a deduction under section 162, there is no requirement under section 212 that the taxpayer be carrying on a continuous or regular activity constituting a trade or business. However, other than the provision for expenditures in connection with the determination, collection, or refund of any tax (presumably not at issue in this memo), the taxpayer's expenditures must be in connection with the production of income, for which a profit motive is still required. Thus, the same considerations for profit motive that apply under section 162 would also apply in the analysis under section 212.

Finally, if expenditures are not deductible under section 162 or section 212, they may nonetheless be deductible, subject to certain limitations, under section 183. Section 183(a) provides that deductions attributable to activities not engaged in for profit are allowable to the extent provided therein. Under section 183(b), two types of deductions are allowable for activities not engaged in for profit: (1) deductions which would be allowable without regard to whether or not such activity is engaged in for profit (i.e., certain taxes); and (2) deductions which would be allowable only if such activity was engaged in for profit, but only to the extent that gross income from the activity exceeds the deductions allowable under (1) above. *See* § 1.183-1(b). Section 183(c) provides that for purposes of section 183, the term "activity not engaged in for profit" means any activity other than one with respect to which deductions are allowable for the taxable year under section 162 or section 212.

To summarize, a taxpayer must be carrying on a trade or business to deduct an expense under section 162. If the taxpayer is not "carrying on" a trade or business, the expenditures may be considered capital or start-up expenditures. If the taxpayer does not meet the "trade or business" requirement, the taxpayer may be permitted to deduct certain expenses under section 212 if it has the requisite profit motive. Finally, if the taxpayer does not carry on a trade or business and does not meet the profit motive test, the taxpayer may be entitled to a limited deduction under section 183.

Whether the Expenditure is "Ordinary"

Whether an expense is ordinary is a variable affected by time, place, and circumstance. *Welch v. Helvering*, 290 U.S. 111, 113 (1933). An expense may be ordinary though it happens but once in the taxpayer's lifetime, yet the transaction that gives rise to it must be of common or frequent occurrence in the type of business involved. *Deputy v. DuPont*, 308 U.S. 488, 495 (1939). One function of the requirement that an expense be "ordinary" is to distinguish currently deductible expenses from capital expenditures. *Commissioner v. Tellier*, 383 U.S. 687, 689 (1966).

No deduction is allowed for capital expenditures, which include amounts paid out for new buildings or for permanent improvements or betterments made to increase the value of any property or estate. Section 263(a)(1). Further, a taxpayer must capitalize the cost of acquisition, construction, or erection of buildings, machinery and equipment, furniture and fixtures, and similar property having a useful life substantially beyond the taxable year. Section 1.263(a)-2(a). Finally, except as otherwise provided in section 1.263(a)-4, a taxpayer must capitalize (i) an amount paid to acquire an intangible; (ii) an amount paid to create an intangible described in section 1.263(a)-4(d); and (iii) an amount paid to create or enhance a separate and distinct intangible asset within the meaning of section 1.263(a)-4(b)(3). Section 1.263(a)-4(b).

The expenditures at issue in this memorandum may be capital expenditures. For example, the taxpayer in Scenario 1 received software from the promoter and deducted the cost under section 162. Costs to acquire computer software from another party in a purchase or similar transaction are capital expenditures under section 1.263(a)-4(c)(xiv), but costs to develop software may be currently deducted under Rev. Proc. 2000-50, 2000-2 C.B. 601. The facts in each scenario would have to be further analyzed to determine whether the costs at issue should be capitalized, either as costs to acquire software or as costs to acquire, create, or enhance tangible or certain intangible property.

Whether the Expenditure is “Necessary”

The Supreme Court has determined that the term “necessary” means “appropriate and helpful in the development of the taxpayer’s business.” *See Welch*, 290 U.S. at 113. The Court also has intimated that expenditures must be reasonable, a determination that is based on facts and circumstances. *See Commissioner v. Heininger*, 320 U.S. 467, 471 (1943). The lower courts have followed up on this concept. In *United States v. Haskel Engineering & Supply Co.*, 380 F.2d 786, 788-89 (9th Cir. 1967), the court stated:

> One requirement, inherent in the concept of "ordinary and necessary" expenses, is that any payment asserted to be allowable as a deduction be reasonable in relation to its purpose. *Commissioner v. Lincoln Electric Co.*, 176 F.2d 815, 817 (6th Cir. 1949). . . . An expenditure may be, by its nature, ordinary and necessary, but at the same time it may be unreasonable in amount. In such a case only the portion which was reasonable would qualify for a deduction under § 162 (a). As the court noted in *Lincoln Electric, supra*, "Clearly it was not the intention of Congress to automatically allow as deductions operating expenses incurred or paid by the taxpayer in an unlimited amount."

The courts have read this reasonableness requirement into various deductions, even when the underlying code section allowing the deduction does not specifically require that the amount be reasonable. *See Lincoln Electric,* 176 F.2d at 817-18. Thus, if the expenditures at issue in this memorandum are not “reasonable,” they are not deductible under section 162.

Whether the Expenditure is an "Expense Paid or Incurred During the Taxable Year"

The payment of cash in exchange for property and services generally constitutes an expense paid or incurred during the taxable year. Amounts also may be treated as paid or incurred during the taxable year if the taxpayer provides property or services (rather than cash) in exchange for property or services (a bartering transaction). Taxpayers that engage in bartering transactions are treated as if they had received cash for their goods or services in an amount equal to the value of goods or services received and then used that cash to purchase goods or services from the other party to the exchange. *See United States v. General Shoe Corp.*, 282 F.2d 9, 12 (6th Cir. 1960). The fair market value of goods or services received must be included in the taxpayer's gross income. Section 1.61-2(d)(1).

If a taxpayer pays partly with cash and partly with services (as in Scenarios 1 and 2), the value of the property and services received by the taxpayer is the difference between the fair market value of property and services received and the amount of cash paid. Thus, for example, if Scenario 1 is otherwise a valid transaction for tax purposes, the taxpayer would be treated as receiving cash in the amount of $ (the value of software and services actually received from the promoter), less $ (amount of cash paid by the taxpayer), for a total amount of $ includible in gross income. The taxpayer would then be treated as paying $ to purchase the software and services and would be allowed to deduct that amount if the requirements of section 162 are otherwise met. *See* Rev. Rul. 73-13, 1973-1 C.B. 42. In addition, the taxpayer would be allowed a deduction for amounts paid or incurred in actually providing services to the promoter. *See* § 1.461-4(d)(4)(ii) for special rules relating to when an accrual method taxpayer may incur a liability arising out of a bartering transaction.

. If $ is significantly more than the fair market value of the provided in Scenario 1, then the expenditure may not be reasonable and, if unreasonable, will not be deductible under section 162 (see discussion above regarding whether the expenditure is "necessary"). Fair market value is defined as the price at which the property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or to sell and both having reasonable knowledge of relevant facts. *E.g., Commissioner v. Marshman*, 279 F.2d 27, 32 (6th Cir. 1960).

Absent evidence to the contrary, the fair market value of what is provided by each side in an arms-length barter transaction is presumed to be equal. *See United States v. Davis*, 370 U.S. 65, 72 (1962).

However, in each scenario addressed in this memo, had an incentive to pay or incur to take full advantage of the section 44 credit. For example, in order for the taxpayer in Scenario 1 to treat $ as paid or incurred when it only actually paid out $, the taxpayer had to include $ in gross income as the value of services provided to the . Thus, the had to set $ as the “fair market value” of its software and services for this transaction to have its intended effect for the taxpayer. Under this set of circumstances, it does not seem appropriate to presume that $ is the fair market value of either the software and services provided by the , or the services and cash provided by the taxpayer.

In addition, there is no evidence that the stated price of the program in each scenario represents the price at which the property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or to sell and both having reasonable knowledge of relevant facts. It seems questionable, for example, that the would pay $ in Scenario 1 for the taxpayer [redacted]

Scenario 3 does not involve a bartering transaction but, instead, involves the payment of cash by the taxpayer and the execution of a promissory note.

Thus, the face amount of the note ($) cannot be deducted under section 162 is not an expense paid or incurred during the taxable year.

<u>Whether the Expenditure is Substantiated</u>

Section 6001 provides that every person liable for any tax imposed by the Code, or for the collection thereof, must keep such records, render such statements, make such returns, and comply with such rules and regulations as the Secretary may from time to time prescribe. The books or records required by section 6001 must be kept at all times available for inspection by authorized internal revenue officers or employees, and must be retained so long as the contents thereof may become material in the administration of any internal revenue law. Section 1.6001-1(e). In order for the taxpayer to deduct the amounts at issue under section 162 (or claim the credit under section 44), the taxpayer must substantiate the amounts of cash paid, as well as the value of any property and services received from the promoter (since that amount is the basis for the taxpayer's deduction).

ISSUE 2

Section 38(a) of the Code provides that there shall be allowed as a credit against tax for the taxable year an amount equal to the sum of – (1) the business credit carryforwards carried to such taxable year, (2) the amount of the current year business credit, plus (3) the business credit carrybacks carried to such taxable year.

Section 38(b) provides that the amount of the current year business credit is the sum of several listed credits determined for the taxable year, including in the case of an eligible small business (as defined in section 44(b)), the disabled access credit determined under section 44(a).

Section 44(a) of the Code allows, in the case of an eligible small business, a credit in an amount equal to 50 percent of so much of the eligible access expenditures for the taxable year as exceed $250 but do not exceed $10,250.

Section 44(b)(1) defines the term "eligible small business" to mean any person if either: (A) the gross receipts of such person for the preceding taxable year did not exceed $1,000,000, or (B) in the case of a person to which subparagraph (A) does not apply, such person employed not more than 30 full-time employees during the preceding taxable year.

Section 44(c)(1) defines the term "eligible access expenditures" to mean amounts paid or incurred by an eligible small business for the purpose of enabling such eligible small business to comply with applicable requirements under the Americans with Disabilities Act of 1990, 42 U.S.C. § 12181 (the ADA) (as in effect on the date of the enactment of section 44).

A taxpayer must be engaged in a trade or business[2] to claim the section 44(a) disabled access credit. The plain meaning of the language in both sections 38 and 44 supports this conclusion. Section 38 clearly and unambiguously provides for a general "business" credit comprised of several credits. Section 44(b)(1) clearly and unambiguously provides that only an eligible small "business" may claim the disabled access credit.

Not all taxpayers engaged in a trade or business are eligible to claim the disabled access credit. Consistent with Congress' intention to alleviate the burden of ADA compliance on small businesses, section 44(b)(1) acts to carve out from among all of

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[2] Whether a taxpayer is engaged in a "trade or business" is discussed in ISSUE 1.

the taxpayers engaged in a trade or business a subset of those who are eligible to claim the disabled access credit. Under section 44(b)(1), an "eligible small business" means any person if either: (A) the gross receipts of such person for the preceding taxable year did not exceed $1,000,000, or (B) in the case of a person to which subparagraph (A) does not apply, such person employed not more than 30 full-time employees during the preceding taxable year.

ISSUE 3

Section 44(a) allows, in the case of an eligible small business, a credit in an amount equal to 50 percent of so much of the eligible access expenditures for the taxable year as exceed $250 but do not exceed $10,250.

Section 44(c)(1) defines the term "eligible access expenditures" to mean amounts paid or incurred by an eligible small business for the purpose of enabling such eligible small business to comply with applicable requirements under the ADA (as in effect on the date of the enactment of section 44).

Section 44(c)(2) provides that the term "eligible access expenditures" includes amounts paid or incurred – (A) for the purpose of removing architectural, communication, physical, or transportation barriers which prevent a business from being accessible to, or usable by, individuals with disabilities, (B) to provide qualified interpreters or other effective methods of making aurally delivered materials available to individuals with hearing impairments, (C) to provide qualified readers, taped texts, and other effective methods of making visually delivered materials available to individuals with visual impairments, (D) to acquire or modify equipment or devices for individuals with disabilities, or (E) to provide other similar services, modifications, materials, or equipment.

Based on the plain language of section 44(c)(1), an eligible small business already in compliance with the ADA may not claim a disabled access credit for expenditures paid or incurred for the purchase of an upgraded or improved auxiliary aid or service because the expenditures are not paid or incurred to enable the eligible small business to comply with the applicable requirements of the ADA. I.R.C. § 44(c)(1); *Fan v. Commissioner*, 117 T.C. 32 (2001) (holding that "petitioner's acquisition of an intraoral camera system did not enable him to comply with the ADA [because] he was already in compliance with the ADA through the use of handwritten notes to communicate with his hearing-impaired patients"). *See also Hubbard v. Commissioner*, T.C. Memo. 2003-245 (finding that, unlike in *Fan*, petitioner was not able to provide vision services to some disabled patients and that the petitioner purchased the automatic refractor and instrument stand to treat disabled patients and to comply with the ADA). Whether an eligible small business is already in compliance with the ADA is a factual issue turning on the particular facts and circumstances of the eligible small business.

ISSUE 4

Section 44(a) allows, in the case of an eligible small business, a credit in an amount equal to 50 percent of so much of the eligible access expenditures for the taxable year as exceed $250 but do not exceed $10,250.

Section 44(c)(1) defines the term “eligible access expenditures” to mean amounts paid or incurred by an eligible small business for the purpose of enabling such eligible small business to comply with applicable requirements under the ADA (as in effect on the date of the enactment of section 44).

Section 44(c)(2) provides that the term “eligible access expenditures” includes amounts paid or incurred – (A) for the purpose of removing architectural, communication, physical, or transportation barriers which prevent a business from being accessible to, or usable by, individuals with disabilities, (B) to provide qualified interpreters or other effective methods of making aurally delivered materials available to individuals with hearing impairments, (C) to provide qualified readers, taped texts, and other effective methods of making visually delivered materials available to individuals with visual impairments, (D) to acquire or modify equipment or devices for individuals with disabilities, or (E) to provide other similar services, modifications, materials, or equipment.

The purpose of the section 44 disabled access credit was to provide “relief to small businesses making the accommodations required by the ADA.” 136 Cong. Rec. S12852 (daily ed. Sept. 12, 1990) (statement by Senator Kohl). See H. Conf. Rept. 101-964, at 1138-1140 (1990). Insofar as an eligible small business recognizes and acts upon the need to provide access to disabled persons, then such business is in compliance with the ADA for purposes of section 44. The fact that the auxiliary aid or service is never, in fact, used should not be determinative.

However, an eligible small business may not claim the disabled access credit under section 44 for expenditures paid or incurred for the purchase of an auxiliary aid or service if under the business’ facts and circumstances the expenditures were not reasonable and necessary to accomplish a purpose described in section 44(c)(2).[3] I.R.C. § 44(c)(3). See *Hubbard v. Commissioner*, T.C. Memo. 2003-245 (finding that in light of the size of petitioner’s practice compared to the cost of the equipment, the benefit to his practice, and the benefit to the community, the purchase of the equipment was reasonable and necessary). An eligible small business is not required to purchase the least expensive method of providing access to disabled individuals. However, the cost must be reasonable in light of the business’ facts and circumstances and necessary to accomplish the purposes of section 44(c)(2). I.R.C. § 44(c)(3).

[3] We note that the requirements of section 44(c)(3) are distinguishable from the criteria for “ordinary and necessary” business expenses under section 162. “Ordinary and necessary” business expenses under section 162 are discussed in ISSUE 1.

ISSUE 5

Section 44(c)(1) defines the term "eligible access expenditures" to mean amounts paid or incurred by an eligible small business for the purpose of enabling such eligible small business to comply with applicable requirements under the ADA (as in effect on the date of the enactment of section 44).

An eligible small business may not claim each taxable year for multiple taxable years a disabled access credit under section 44 for expenditures paid or incurred for annual subscriptions to Programs 1 or 2 because such annual subscription costs constitute an attempt to circumvent the limitation imposed by section 44(c)(1). Under section 44(c)(1), an eligible small business already in compliance with the ADA may not claim a disabled access credit for subsequent expenditures for the same purpose because the expenditures are not paid or incurred to enable the eligible small business to comply with the applicable requirements of the ADA. I.R.C. § 44(c)(1); *Fan*, 117 T.C. 32. It is arguable that by purchasing annual subscriptions in Programs 1 or 2 the purchasing taxpayers are attempting to circumvent this limitation for the purpose of generating disabled access credits. At the end of each year, the termination of a taxpayer's subscription will cause the taxpayer to fall out of compliance with the ADA. The taxpayer will purchase another annual subscription thereby generating another $5,000 disabled access credit. We believe that a strong argument can be made that such repeat expenditures with respect to Programs 1 and 2 are unreasonable and unnecessary to accomplish the purpose of providing an effective method of making aurally delivered materials available to individuals with hearing impairments. I.R.C. § 44(c)(3).

ISSUES 6 AND 7

The Department of Justice has primary enforcement authority for and has promulgated regulations and a Technical Assistance Manual interpreting the Americans with Disabilities Act of 1990, 42 U.S.C. § 12181 (the ADA). 28 C.F.R. Pt. 36; The Americans with Disabilities Act Title III Technical Assistance Manual (November 1993). Accordingly, whether an eligible small business must have a physical structure into which the public enters in order to meet the ADA's "place of public accommodation" requirement and what the ADA requires of a particular eligible small business found to be subject to its tenants are both issues within the Department of Justice's jurisdiction.

Place of Public Accommodation

The following is general information on the treatment of the "place of public accommodation" issue thus far.

Section 12182(a) of the ADA provides that, in general, Title III prohibits discrimination against an individual on the basis of disability in the full and equal enjoyment of the goods, services, facilities, privileges, advantages, or accommodations of any place of public accommodation by any person who owns, leases (or leases to), or operates a place of public accommodation. 42 U.S.C. § 12182(b)(1); 28 C.F.R. § 36.201.

Section 12181(7) of the ADA provides that the term "place of public accommodation" means a facility, operated by a private entity, whose operations affect commerce and fall within at least one of the 12 broad categories of facilities listed in the statute. 28 C.F.R. § 36.104.

Section 36.104 of the regulations under the ADA provides that the term "public accommodation" means a private entity that owns, leases, or operates a "place of public accommodation."

Section 36.104 provides that the term "facility" means all or any portion of buildings, structures, sites, complexes, equipment, rolling stock or other conveyances, roads, walks, passageways, parking lots, or other real or personal property, including the site where the building, property, structure, or equipment is located.

Congress has clearly defined the purpose of the ADA. The purpose is to provide a clear and comprehensive national mandate for the elimination of discrimination against individuals with disabilities; to provide clear, strong, consistent, enforceable standards addressing discrimination against individuals with disabilities; to ensure that the Federal Government plays a central role in enforcing the standards established in the ADA on behalf of individuals with disabilities; and to invoke the sweep of Congressional authority in order to address the major areas of discrimination faced day-to-day by people with disabilities. 42 U.S.C. § 12111(b).

Based on the majority of case law interpreting the ADA, it appears that the term "place of public accommodation" is limited to actual physical structures. A nexus between the challenged service and the premises of a physical public accommodation is required. Further, it appears that the definition of "public accommodation" is not limited to entities providing services "at" the public accommodation. In other words, the services "of" a public accommodation do not have to be provided "at" the public accommodation to fall under the ADA.[4] Finally, based on the regulations issued by the Department of Justice,

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[4] *See, e.g., Stoutenborough v. National Football League, Inc.*, 59 F.3d 580 (6th Cir. 1995) (finding that the broadcast of NFL games was not a service of the football stadium, the only identifiable public accommodation); *Parker v. Metropolitan Life Insurance Company*, 121 F.3d 1006 (6th Cir. 1997) (finding that "a public accommodation is a physical place" and that a benefit plan offered by an employer is not a good offered by a place of public accommodation); *Ford v. Schering-Plough Corporation*, 145 F.3d 601 (3rd Cir. 1998) (finding that a public accommodation is a place and that because the plaintiff "received her disability benefits via her employment, she had no nexus to an 'insurance office' and thus was not discriminated against in connection with a public accommodation"); *Pallozzi v. Allstate Life Ins. Co.*, 198 F.3d 28 (2d Cir. 1999) (finding that Title III prohibits an insurance office from discriminatorily refusing to offer its policies to disabled persons and noting that, unlike in *Parker* and

it appears that the term “place of public accommodation” includes only those areas of a business entered into and used by customers and clients. *See* 28 C.F.R. § 36.207 and 28 C.F.R. Pt. 36, App. B (explaining what portions of a private residence constitute a public accommodation); 28 C.F.R. § 104 and 28 C.F.R. Pt. 36, App. B. (explaining what portions of a commercial facility constitute a public accommodation).

Applicable Requirements under the ADA

The following is general information on the requirements of Title III of the ADA. This information is not comprehensive.

Section 44(c)(1) defines the term “eligible access expenditures” to mean amounts paid or incurred by an eligible small business for the purpose of enabling such eligible small business to comply with applicable requirements under the ADA (as in effect on the date of the enactment of section 44).

Section 12182(a) and (b)(1) of the ADA contains Title III’s general non-discrimination provisions. Section 12182(a) provides that no individual shall be discriminated against on the basis of disability in the full and equal enjoyment of the goods and services, facilities, privileges, advantages, or accommodations of any place of public accommodation by any person who owns, leases (or leases to) or operates a place of public accommodation. Section 12182(b)(1) provides that:

Ford where the plaintiffs obtained benefits through their employers, not from an insurance office, plaintiffs in this case had a nexus to a place of public accommodation, Allstate’s insurance office.); *Weyer v. Twentieth Century Fox Film Corporation*, 198 F.3d 1104 (9th Cir. 2000) (finding that all the public accommodations listed in § 12181(7) have something in common in that they are actual, physical places where goods or services are open to the public, and places where the public gets those goods or services); *Rendon v. Valleycrest Production Limited*, 294 F.3d 1279 (11th Cir. 2002) (finding that the Who Wants to Be A Millionaire show takes place at a public accommodation within the meaning of section 12181(7)(C) covering theaters and that *Weyer*, *Ford*, and *Parker*, “do not stand for the broad proposition that a place of public accommodation may exclude persons with disabilities from services or privileges performed within the premises of the public accommodation so long as the discrimination itself occurs off site or over the telephone”); *Hooks v. OKBridge, Inc.*, No. 99-214 (W.D. Tex. Aug. 4, 1999) (granting summary judgment against the plaintiff because OKBridge provided services over the internet rather than a physical place). *Contra Carparts Distribution Center, Inc. v. Automotive Wholesaler’s Association of New England, Inc.*, 37 F.3d 12 (1st Cir. 1994) (finding that “the plain meaning of the terms [in section 12181(7)] do not require ‘public accommodations’ to have physical structures for persons to enter” and explaining that “[m]any travel services conduct business by telephone or correspondence without requiring their customers to enter an office in order to obtain their services”).

> (i) It shall be discriminatory to subject an individual or class of individuals on the basis of a disability or disabilities of such individual or class, directly, or through contractual, licensing, or other arrangements, to a denial of the opportunity of the individual or class to participate in or benefit from the goods, services, facilities, privileges, advantages, or accommodations of an entity;
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> (ii) It shall be discriminatory to afford an individual or class of individuals, on the basis of a disability or disabilities of such individual or class, directly, or through contractual, licensing, or other arrangements with the opportunity to participate in or benefit from a good, service, facility, privilege, advantage, or accommodation that is not equal to that afforded to other individuals; and
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> (iii) It shall be discriminatory to provide an individual to provide an individual or class of individuals, on the basis of a disability or disabilities of such individual or class, directly, or through contractual, licensing, or other arrangements with a good, service, facility, privilege, advantage, or accommodation that is different or separate from that provided to other individuals, unless such action is necessary to provide the individual or class of individuals with a good, service, facility, privilege, advantage, or accommodation, or other opportunity that is as effective as that provided to others.

Section 12182(b)(2) sets forth specific examples of discrimination under Title III. Section 12182(b)(2) provides that for purposes of section 12182(a), discrimination includes:

> (i) the imposition or application of eligibility criteria that screen out or tend to screen out an individual with a disability or any class of individuals with disabilities from fully and equally enjoying any goods, services, facilities, privileges, advantages, or accommodations, unless such criteria can be shown to be necessary for the provision of the goods, services, facilities, privileges, advantages, or accommodations being offered;
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> (ii) a failure to make reasonable modifications in policies, practices, or procedures, when such modifications are necessary to afford such goods, services, facilities, privileges, advantages, or accommodations to individuals with disabilities, unless the entity can demonstrate that making such modifications would fundamentally alter the nature of such goods, services, facilities, privileges, advantages, or accommodations;
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> (iii) a failure to take such steps as may be necessary to ensure that no individual with a disability is excluded, denied services, segregated or otherwise treated differently than other individuals because of the absence of auxiliary aids and services, unless the entity can demonstrate that taking such steps would fundamentally alter the nature of the good, service, facility, privilege, advantage, or accommodation being offered or would result in an undue burden;

> (iv) a failure to remove architectural barriers, communication barriers that are structural in nature, in existing facilities, and transportation barriers in existing vehicles and rail passenger cars used by an establishment for transporting individuals (not including barriers that can only be removed through the retrofitting of vehicles or rail passenger cars by the installation of a hydraulic or other lift), where such removal is readily achievable; and
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> (v) where an entity can demonstrate that the removal of a barrier under clause (iv) is not readily achievable, a failure to make such goods, services, facilities, privileges, advantages, or accommodations available through alternative methods if such methods are readily achievable.

Section 12181(9) defines the term "readily achievable" to mean easily accomplishable and able to be carried out without much difficulty or expense. In determining whether an action is readily achievable, factors to be considered include:

> (A) the nature and cost of the action needed;
>
> (B) the overall financial resources of the facility or facilities involved in the action; the number of persons employed at the facility; the effect on expenses and resources, or the impact otherwise of such action upon the operation of the facility;
>
> (C) the overall financial resources of the covered entity; the overall size of the business of a covered entity with respect to the number of its employees; the number, type, and location of its facilities; and
>
> (D) the type of operation or operations of the covered entity, including the composition, structure, and functions of the workforce of such entity; the geographic separateness, administrative or fiscal relationship of the facility or facilities in question to the covered entity.

Amounts paid or incurred by an eligible small business to purchase Programs 1, 2, or 3 do not meet the definition of "eligible access expenditures" under section 44(c) if the expenditures were not paid or incurred to enable the eligible small business to comply with the applicable requirements under the ADA. *Fan*, 117 T.C. 32 (concluding under the facts and circumstances of the case at bar that if the expenditure was not made to enable compliance with the ADA, then the expenditure does not qualify for the credit under section 44). What the ADA requires of a particular eligible small business depends upon the application of the particular eligible small business' facts and circumstances to the requirements in the ADA. For example, whether the product or service was designed to address particular concerns of the disabled or whether the product or service has general applicability and usefulness[5] to all clients and customers purchased in the normal course of business should be considered. Further, whether the primary benefit of the product or service was to the eligible small business with incidental or ancillary benefits to the disabled should also be considered.

Please call if you have any further questions.

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[5] The fact that both disabled and non-disabled individuals use and benefit from a product or service is not by itself fatal to a claim for the disabled access credit. *Hubbard*, T.C. Memo. 2003-245. However, whether both disabled and non-disabled individuals use and benefit from a product or service may be one factor in determining whether the product or service was purchased to comply with the applicable requirements of the ADA. *Fan*, 117 T.C. 32 (holding that the taxpayer was not entitled to the disabled access credit and finding in part that the plaintiff did not limit use of the intraoral camera system to his hearing-impaired patients).