



BY JIM DAVIDSON

## Eating Our Seed Corn

*According to a recent report, the pharmaceutical industry is considering giving up its business expense deduction for the cost of advertising. It's a "troubling" development, our Capitol Hill observer reports.*

A few years ago, some members of Congress began to suggest that the government could raise significant new tax revenues if it were to disallow a percentage of the amount that companies deduct as an ordinary and necessary business expense. When asked what he thought about the proposal, the chairman of the powerful House Ways and Means Committee, Rep. Dan Rostenkowski, responded, "That is like a farmer eating his seed corn." Quite simply, it would be taking away your ability to plant new corn or to survive in the future.

Nevertheless, an economic research firm has reported that "Congress" has approached the pharmaceutical industry and asked for approximately \$100 billion over 10 years as the industry's contribution toward the cost of healthcare reform. "Behind closed doors, drug company CEOs and their trade organization, PhRMA... are actively discussing how and what they might 'voluntarily' contribute." Apparently they are considering offering up the business expense deduction for the cost of advertising.

We would be troubled if this industry, like Hester Prynne, would offer up the deduction as a form of penance, agreeing to wear the scarlet "A" (for Advertising) to acknowledge past sins in order to pursue a new life of penance and dignity. Even if it is true – it would be small penance (\$910 million a year), and it could create a precedent that Congress may choose to apply to other industries. Given the state of our nation's economy, no business could afford a "tax" on its ability to sell its products. Let's analyze this issue and the facts surrounding it to add some perspective.

- It would be in fact small penance. The pharmaceutical industry in 2008 spent a reported amount of approximately \$4.34 billion on print and broadcast advertising of prescription medications. The real amount paid after advertising discounts appears to be closer to \$2.6 billion. Assuming for the moment that companies paid the maximum 35 percent corporate income tax on their profits, the elimination of the deduction for the \$2.6 billion

expense would amount to \$910 million a year, or approximately \$9.1 billion over 10 years in current dollars.

- Moreover, an offer to give up the deduction of all advertising costs could be a particularly dangerous strategy for a company that has an extensive line of over the counter medicines. While it would constitute a significant increase in taxes to forego the deduction for prescription medicine advertising, it could create havoc for a company's business plan if *all* of its advertising were to lose the deduction.
- If there were an assumption that a denial of the deduction for advertising costs would result in less advertising of prescription medications, does that suggest that both pharmaceutical companies that support the lost deduction and the Congress believe there is no value to consumers in the advertising? The facts seem to be to the contrary. Sixteen million of the 60 million Americans who have high blood pressure are unaware they have this disease. But a trip to the doctor prompted by one ad could put a consumer on a path to better health.
- The U.S. Supreme Court for 35 years has continued to strengthen the protection for DTC advertising from government restrictions, and that likely would include discriminatory tax policy.
- Finally the precedent for other industries and advertisers could be staggering. For more than 20 years, advertisers and the advertising and media industries successfully have defeated proposals put forward in the Congress to tax or restrict advertising and its content. Even amendments that repeatedly were offered to deny the tobacco industry the deduction for the cost of advertising tobacco products were defeated resoundingly in the Senate. If an industry as visible as the pharmaceutical industry were to offer up its advertising for taxation, this could lead to a similar request being made of the public power industry, the food industry, the airline industry, the credit card industry, and even the struggling automobile industry.

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