

BEFORE THE TAX COMMISSION OF THE STATE OF IDAHO

In the Matter of the Protest of)	
)	DOCKET NO. 13418
[Redacted],)	
)	DECISION
Petitioner.)	
_____)	

The petitioner protests the Notice of Deficiency Determination issued by the auditor for the Idaho State Tax Commission (Commission) dated January 27, 1999, making adjustments to the income and deductions reported for 1995 and 1996. Although numerous adjustments were made by the auditor, no additional income taxes, penalties, or interest were asserted against the petitioner since the petitioner is an S corporation.

The petitioner is wholly owned by [Redacted]. Both [Redacted] were also employed by the petitioner.

The auditor made numerous adjustments to the petitioner's Idaho income tax returns. These adjustments included amounts deducted as insurance, entertainment, rent, auto expense, cost of goods sold, and many others. Some additional documentation has been submitted to further support some of the claimed deductions. Therefore, the Commission now renders its decision based upon the information in the file at this time.

The first adjustment made by the auditor for 1995 was to reduce the amount claimed as "repairs" by \$1,256.49. This adjustment was composed of two items. The first was an amount paid to "[Redacted]" which the auditor deemed to be personal. The second item was "laundry expense" in the amount of \$1,103.00.

It appears that no additional documentation was submitted regarding the expenditure to [Redacted]. For the laundry expense, the petitioner submitted a letter from a laundry stating that

the laundry charged \$2.00 per pound to launder rags. The petitioner contends that it would have needed to launder 1,200 pounds of rags in a given year and that, therefore, a deduction of \$2,400.00 should be allowed rather than the \$1,103.00 initially claimed.

The Commission finds that the petitioner's argument lacks merit. The petitioner is a cash basis taxpayer. Therefore, deductions are generally allowed when the expense is paid. The petitioner has not demonstrated that it incurred a laundry expense in any amount. Therefore, the auditor's adjustment in the amount of \$1,256.49 is affirmed.

"Repairs" claimed by the petitioner for 1996 appear to include repairs to the [Redacted] hot tub, repairs to their washer, and the cost of a maintenance agreement for a gas powered blower presumably used in conjunction with maintaining the grounds of the shareholders' residence. The claimed expenses also included expenditures for heating or air conditioning maintenance, again presumably for the shareholders' residence and an unidentified payment to a motorcycle vendor. The Commission finds no substantial basis for the allowance of a business deduction with regard to these claimed expenditures.

Many of the deductions sought by the petitioner have to do with an office in the home of [Redacted], the sole shareholders of the petitioner. The petitioner claimed a wide variety of such expenses. The expenses were characterized largely as either "office expense" or "supplies." These expenses included artwork, expenses for dog food and grooming, lawn and garden items, appliances, and furniture, among other things. The Commission finds that these items are not deductible by the petitioner.

The "office" in question was rented to the petitioner by the [Redacted].

Internal Revenue Code § stated, in part:

Disallowance of certain expenses in connection with business use of home, rental of vacation homes, etc.

(a) General rule.

Except as otherwise provided in this section, in the case of a taxpayer who is an individual or an S corporation, no deduction otherwise allowable under this chapter shall be allowed with respect to the use of a dwelling unit which is used by the taxpayer during the taxable year as a residence.

* * *

(c) Exceptions for certain business or rental use; limitation on deductions for such use.

(1) Certain business use. Subsection (a) shall not apply to any item to the extent such item is allocable to a portion of the dwelling unit which is exclusively used on a regular basis –

(A) [as] the principal place of business for any trade or business of the taxpayer.

(B) as a place of business which is used by patients, clients, or customers in meeting or dealing with the taxpayer in the normal course of his trade or business, or

(C) in the case of a separate structure which is not attached to the dwelling unit, in connection with the taxpayer's trade or business.

In the case of an employee, the preceding sentence shall apply only if the exclusive use referred to in the preceding sentence is for the convenience of his employer.

* * *

(3) Rental use. Subsection (a) shall not apply to any item which is attributable to the rental of the dwelling unit or portion thereof (determined after the application subsection (e)).

* * *

(6) Treatment of rental to employer. Paragraphs (1) and (3) shall not apply to any item which is attributable to the rental of the dwelling unit (or any portion thereof) by the taxpayer to his employer during any period in which the taxpayer uses the dwelling unit (or portion) in performing services as an employee of the employer.

* * *

(d)(2) Personal use of unit. For purposes of this section, the taxpayer shall be deemed to have used a dwelling unit for personal purposes for a day if, for any part of such day, the unit is used –

- (A) for personal purposes by the taxpayer or any other person who has an interest in such unit, or by any member of the family (as defined in section 267(c)(4) of the taxpayer or such other person;
- (B) by any individual who uses the unit under an arrangement which enables the taxpayer to use some other dwelling unit (whether or not a rental is charged for the use of such other unit; . . .

* * *

(f)(2) Personal use by shareholders of S corporation. In the case of an S corporation, subparagraphs (A) and (B) of subsection (d)(2) shall be applied by substituting "any shareholder of the S corporation" for "the taxpayer" each place it appears.

Since the dwelling unit was used continuously as a residence by the shareholders of the petitioner, the deductions sought regarding the office in the home of the [Redacted] are denied.

In 1995, the petitioner purchased tickets from "Professional Fire Fighter of Idaho." Nothing on the tickets indicate the nature of the purchase. The tickets are clearly marked "TICKET PURCHASES ARE NOT TAX DEDUCTIBLE." For some of the tickets, the petitioner contends that it didn't use the tickets. Therefore, petitioner contends that it should be allowed a deduction for the purchase price of the tickets. There was also no representation that the value of the tickets was less than the amount paid. The Commission finds that the petitioner has failed to demonstrate that these expenditures qualified to be deductible as charitable contributions. Revenue Ruling 67-246, 1967-2 CB 104; Urbauer v. Commissioner, T. C. Memo 1992-170.

Numerous expenditures were claimed for meal expenses. The majority of these were disallowed by the auditor due to lack of the documentation required by Internal Revenue Code § 274. Even though one's meals are not otherwise deductible, they may qualify as travel and entertainment if they are properly documented. Treasury Regulation 1.274-5T states, in part, the following:

Elements of an expenditure or use – (1) In general. Section 274(d) and this section contemplate that no deduction or credit shall be allowed for any expenditure for travel, entertainment, a gift, or with respect to listed property unless the taxpayer substantiates the following elements for each such expenditure:

* * *

Entertainment in general. Elements to be proved with respect to an expenditure for entertainment are–

(i) Amount. Amount of each separate expenditure for entertainment, except that such incidental items as taxi fares or telephone calls may be aggregated on a daily basis;

(ii) Time. Date of entertainment;

(iii) Place. Name, if any, address or location, and designation of type of entertainment, such as dinner or theater, if such information is not apparent from designation of the place;

(iv) Business purpose. Business reason for the entertainment or nature of business benefit derived or expected to be derived as a result of the entertainment and, except in the case of business meals described in section 274(e)(1), the nature of any business discussion or activity;

(v) Business relationship. Occupation or other information relating to the person or persons entertained, including name, title, or other designation, sufficient to establish business relationship to the taxpayer.

The regulation goes on to specify that the record should be made at or near the time of the expenditure. The Commission finds that the petitioner has failed to meet the documentation requirements of Internal Revenue Code § 274. Therefore, the deductions are limited to those allowed by the auditor.

In addition to the meals, many other expenditures were deducted which appear to have been personal expenses. The petitioner deducted such things as the cost of a shareholder's driver's license, clothing, a wallet, vitamins, shoes, and underwear. Some of the receipts lacked sufficient information to be able to determine the nature of the purchase. Other receipts were labeled, for example, "for workers." One such receipt from Albertsons labeled "for workers" included milk, cookies, brown eggs, two purchases of diapers, cereal, and floral. The

Commission finds that the petitioner has failed to carry its burden of showing that such expenses are legitimately deductible. Internal Revenue Code § 262.

The petitioner contested the adjustment made by the auditor to the telephone expense claimed. There was a telephone line to the stockholders' home. There was also a cell phone used. The auditor has indicated that she allowed all of the expense for the cell phone but denied the expense for the phone to the shareholders' residence. The petitioner contends that it is entitled to a deduction for a second phone line in the shareholders' home that was not allowed by the auditor. The expense of the second telephone should be deductible to the extent of business use of this telephone. The record before the Commission lacks proof of this fact. The Commission finds that this telephone line is regarded by the telephone company as a residential line rather than a business line. Further, the Commission finds no listing for the petitioner in the telephone books in either the business listings or the yellow pages. The petitioner did have several employees and subcontractors involved in the cleaning business. Therefore, presumably, there was some business use of the telephone. The Commission finds that half of this additional expense should be allowed as a deduction.

The petitioner requests an additional deduction for 1995 and 1996 for rags purchased for cleaning in the amounts of \$75.26 and \$119.74, respectively. The Commission finds this allowable based upon the information provided.

The petitioner claims that the deduction for workmen's compensation should be increased from the amount originally claimed on its income tax returns. Additional documentation was submitted to support this contention. Upon examining this information, the Commission finds that the additional amount is warranted.

The petitioner asks that the expenses of a 1971 Buick be allowed since employees of the petitioner used the vehicle. The petitioner has not submitted documentation that the petitioner owned such a vehicle or to establish the portion of the use of the vehicle which might be business related. Therefore, the Commission finds that no modification of the auditor's report need be made with regard to this vehicle.

WHEREFORE, the Notice of Deficiency Determination dated January 27, 1999, is MODIFIED and, as so modified, is hereby APPROVED, AFFIRMED, AND MADE FINAL.

An explanation of the petitioner's right to appeal this decision is enclosed with this decision.

DATED this ____ day of _____, 2001.

IDAHO STATE TAX COMMISSION

COMMISSIONER

CERTIFICATE OF SERVICE

I hereby certify that on this ____ day of _____, 2001, a copy of the within and foregoing DECISION was served by sending the same by United States mail, postage prepaid, in an envelope addressed to:

[REDACTED]Receipt No. [Redacted]
[REDACTED][REDACTED]
[REDACTED][REDACTED][REDACTED]

ADMINISTRATIVE ASSISTANT 1