OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

In the Matter of the Appeal of:	)	OTA Case No. 18010735
	)	
DEWAYNE HARMON	)	Date Issued: June 18, 2018
	)	
	)	
	)	

OPINION

Representing the Parties:

For Appellant — Tax Appeals Assistance Program (TAAP)[1]

For Respondent: — Rachel Abston, Senior Legal Analyst

THOMPSON, Administrative Law Judge: Pursuant to California Revenue and Taxation Code section 19045,[2] Dewayne Harmon (appellant) appealed the action of the Franchise Tax Board (FTB or respondent) on his protest of a proposed assessment of $3,235.00 in additional tax and a $722.25 late-filing penalty, plus applicable interest, for the 2011 tax year.

Appellant did not request an oral hearing and therefore the matter is being decided based on the written record.

ISSUES

1. Was FTB's proposed assessment issued within the statute of limitations?
2. Is appellant entitled to a claimed unreimbursed employee expense deduction of $38,608?
3. Is appellant liable for the late-filing penalty?

[1] Appellant filed his own appeal letter. Ron Simmons of TAAP submitted a declaration on TAAP letterhead that is signed by appellant. TAAP did not submit any briefs.

[2] Unless otherwise indicated, all "Section" references are to sections of the California Revenue and Taxation Code.

FACTUAL FINDINGS

1. Appellant resided in Santa Rosa, California, during the year at issue. He worked for Cove Construction, which had an office in San Anselmo, California.
2. On January 7, 2013, appellant filed a California Resident Income Tax Return for the 2011 tax year. Appellant reported wages of $107,384 and California itemized deductions of $38,580.
3. Appellant claimed unreimbursed expenses included a $38,608 mileage expense based on 72,714 business miles driven during 2011.
4. FTB audited appellant's itemized deductions. Only the mileage expense remains at issue in this appeal.
5. During audit, FTB requested, among other things, a copy of the employer's policy or contract regarding expense reimbursement, information about the identity of the employer, a detailed schedule of each unreimbursed business expense including the amount of each expense and a description of the activity and business purpose, and a detailed transportation log.
6. Appellant provided bank statements showing numerous charges at gas stations during 2011. The bank statements do not show how much of the charges were related to appellant's regular commute, personal travel or other personal expenses.
7. Appellant did not provide a log or other contemporaneous record-keeping of where and when he drove and the mileage associated with the driving.
8. Appellant did not provide evidence to substantiate beginning and ending odometer readings.
9. On April 14, 2016, FTB issued a Notice of Proposed Assessment (NPA) proposing to disallow the itemized deductions due to lack of substantiation. The NPA also proposed a late-filing penalty of $722.25
10. On May 16, 2016, appellant protested the proposed assessment. He argued that his employer required him to buy tools, supplies and meals, and stated that he tried to find records but the employer no longer existed.
11. On October 18, 2016, FTB sent appellant a letter stating that appellant's claimed mileage expense deduction of $38,608 would be disallowed due to lack of adequate substantiation. As a result of this disallowance, FTB allowed appellant to claim the

standard deduction, since it was greater than the amount of appellant's California itemized deductions (as revised). FTB requested that, if appellant still disagreed with its determination, appellant provide a detailed business mileage log satisfying the requirements of Internal Revenue Code (IRC) section 274(d) and listing locations, date and business purpose for each event.

12. On January 6, 2017, FTB issued a Notice of Action affirming its NPA.

13. Appellant then filed this timely appeal.

DISCUSSION

Issue 1 – Was FTB's proposed assessment issued within the statute of limitations?

On appeal, appellant contends that FTB's assessment is barred by the statute of limitations. However, this is not the case. Appellant did not file his 2011 tax return until January 7, 2013, and FTB had four years from that date, to January 7, 2017, to propose additional tax. (§ 19057.) FTB issued its proposed assessment on April 14, 2016, so the assessment is not barred by the statute of limitations.

Issue 2 – Is appellant entitled to a claimed unreimbursed employee expense deduction of $38,608?

The taxing agency's determination that an item is not deductible is presumed correct, and the taxpayer has the burden of proving it to be wrong. (*Smith v. Comm'r* (9th Cir. 2002) 1023, 1029; *Appeal of James C. and Monablanche A. Walshe*, 75-SBE-073,[3] Oct. 20, 1975.) A taxpayer must retain sufficient records to substantiate claimed deductions. (*Sparkman v. Comm'r* (9th Cir. 2007) 509 F.3d 1149, 1159 (*Sparkman*); Treas. Reg. § 1.6001-1(a).)

IRC section 274(d) imposes strict substantiation requirements for certain types of expenses, including business mileage.[4] Among other things, IRC section 274(d) does not allow

[3] Pursuant to the Office of Tax Appeals Rules for Tax Appeals, California Code of Regulations, tit. 18, § 30501(d)(3), precedential opinions of the State Board of Equalization (BOE) that were adopted prior to January 1, 2018, may be cited as precedential authority to the Office of Tax Appeals unless a panel removes, in whole or in part, the precedential status of the opinion. BOE's precedential opinions are available for viewing on the BOE's website: www.boe.ca.gov/legal/legalopcont.htm.

[4] As relevant here, IRC section 274(d) is incorporated into California law by Section 17071.

the amount of expenses to be estimated under what is known as the *Cohan* rule.[5] (See, e.g., *Fleming v. Comm'r*, T.C. Memo. 2010-60.) IRC section 274(d) requires a taxpayer to substantiate expenses by adequate records or other corroborating evidence of (1) the amount of each use (here, the mileage), (2) the time and place of the use, and (3) the business purpose of the use. The Tax Court explains that: "Generally, expenses subject to the strict substantiation requirements of [IRC] section 274(d) must be disallowed in full unless the taxpayer satisfies every element of those requirements." (*Fleming, supra*.)

Federal regulations provide that taxpayers will have maintained "adequate records" if they maintain a contemporaneous log or diary, combined with supporting documents, which substantiate the required elements of the expense, such as the amount, date and business purpose of the item. (Treas. Reg. § 1.274-5T(c)(2)(i).) If "adequate records" are not provided under this provision, the taxpayer must establish each element of the expense by his own statement containing specific detail as to each element, and "other corroborative evidence sufficient to establish such element," or other evidence, with respect to each element, possessing "the highest degree of probative value possible under the circumstances …." (*Id.*)

Generally, commuting expenses between one's home and regular place of work are not deductible. (*Bogue v. Comm'r*, T.C. Memo. 2011-164.) If an employee temporarily works at locations that are distant from the employee's regular employment, travel expenses to the temporary location may be deductible. (*Ibid*.) However, such expenses will not be deductible if the temporary work locations are in the same general area as the taxpayer's regular employment. (*Ibid*.)

In response to FTB's appeal brief, appellant provides a declaration stating that he previously had receipts for all expenses deducted but that, after an exhaustive search, he was unable to locate the records. However, it is the taxpayer's obligation to maintain adequate records to substantiate a deduction. (See, e.g., *Dorrance v. United States* (9th Cir. 2015) 809 F.3d 479, 484; *Sparkman, supra*, 509 F.3d at p. 1159.) If such evidence is unavailable, it is "the

[5] In some circumstances, expenses may be estimated under what is commonly referred to as the *Cohan* rule. (See *Cohan v. Comm'r* (2d Cir. 1930) 39 F.2d 540, 543-544.) However, IRC section 274(d) supersedes the *Cohan* rule with respect to certain expenses, such as the mileage expense at issue here. Therefore, the *Cohan* rule cannot be applied.

taxpayer, not the government, [that] suffers the consequence."[6] (*Talley Industries Inc. v. Comm'r* (9th Cir. 1997) 116 F.3d 382, 387-388.)

During audit and protest proceedings at FTB, appellant made an effort to locate and provide substantiating documentation. However, the documents provided to FTB (which were later submitted in this appeal) were not combined with a log or other contemporaneous record-keeping and do not provide sufficient detail and corroborating evidence to establish each of the required elements for the transportation expenses (i.e., the amount of mileage, the dates and destinations, and the business purpose for each use). For example, appellant provided charge records from gas stations, but the charges vary widely from month to month, and there is no basis to determine what portion of the charges relate to personal travel or commuting, as opposed to business mileage. In addition, there is no documentation of odometer readings showing the actual miles driven.[7] As noted above, IRC section 274(d) does not allow the estimation of the mileage expenses, even if such an estimation were possible.

In addition, appellant has not demonstrated what portion of the mileage, if any, consists of travel to temporary worksites that are distant from the area of appellant's regular employment. Appellant stated at audit that he would first drive from Santa Rosa to the office of Cove Construction in San Anselmo, and then to Tiburon. However, we have no evidence to substantiate appellant's contention that he first drove to San Anselmo instead of driving directly to job sites. In any event, if appellant did in fact regularly drive to his employer's San Anselmo office, the drive would be considered part of appellant's regular commute and would not be deductible.

During the audit, appellant provided a statement from a Tiburon homeowner stating that appellant drove his personal truck to the homeowner's Tiburon home five days a week for more than two years, including 2011, in order to build the homeowner's house. This broad statement

[6] Treasury Regulation section 1.274-5T(c)(5) provides a limited exception where the taxpayer shows that records were lost due to circumstances beyond the taxpayer's control, such as a fire, and the taxpayer is able to reasonably reconstruct the records. While appellant states his employer went out of business, there is no evidence of a fire or other circumstances outside of appellant's control that destroyed his records. Moreover, it is appellant's obligation to retain sufficient records to substantiate his claimed deductions, not his employer's obligation. Therefore, this exception is not applicable.

[7] Appellant provided his federal Form 2106, which lists the total miles appellant claims he drove during 2011 (87,714) and the total claimed business miles (72,714) for which he seeks a deduction. However, "[a] tax return, even though signed under penalty of perjury, is not per se evidence of the income, deductions, credits, and other items claimed therein." (*Sparkman*, *supra*, 509 F.3d at pp. 1156–57.)

is dated more than three years after the year at issue and is not signed under penalty of perjury or corroborated by other evidence of daily travel to Tiburon.[8] In the absence of corroborating evidence, we question whether appellant drove to Tiburon every business day for more than two years in order to build a home. Moreover, Tiburon is not distant from San Anselmo and is part of the same general area where appellant states that he regularly worked. As a result, any mileage to Tiburon would also constitute a part of appellant's non-deductible regular commuting expenses. (See *Bogue, supra*.) Appellant states generally that he drove to additional sites throughout the San Francisco Bay Area, but we do not have evidence of the locations and dates of travel and therefore have no basis to determine that any such expenses are deductible.

Appellant states he has been suffering from health difficulties and that he has been unemployed. He requests that his tax debts be forgiven. We are sympathetic to appellant's situation, but we do not have statutory authority to grant a hardship exemption or waiver from appellant's tax obligation. Following this appeal, appellant may wish to contact FTB to learn about any programs that might be able to provide assistance, such as FTB's Offer in Compromise program or payment plans.[9]

Issue 3 – Is appellant liable for the late-filing penalty?

Section 19131 imposes a late-filing penalty for failure to file a tax return by its due date, unless the taxpayer shows that the late filing was due to reasonable cause and not due to willful neglect. To establish that the late filing was due to reasonable cause, a taxpayer must show that the failure to file a timely return "occurred despite the exercise of ordinary business care and prudence, or that cause existed as would prompt an ordinary intelligent and prudent businessman to have so acted under similar circumstances." (*Appeal of Howard G. and Mary Tons*, 79-SBE-027, Jan. 9, 1979.)

Here, it is not disputed that appellant filed his tax return late. He asks that the late-filing

[8] Treasury Regulation section 1.274-5T(c)(1) provides that contemporaneous records have "a high degree of credibility not present with respect to a statement prepared subsequent thereto when generally there is lack of sufficient recall." For this reason, "the corroborative evidence required to support a statement not made at or near the time of the expenditure or use must have a high degree of probative value to elevate such statement ... to the level of credibility reflected by a [contemporaneous record supported by sufficient documentary evidence]."

[9] FTB will only consider such matters after a tax liability has become final. For more information about payment plans, see https://www.ftb.ca.gov/online/eia/index.asp?WT.mc_id=Ind_Pay_eIA or call FTB at (800) 689-4776. For more information regarding Offers in Compromise, see https://www.ftb.ca.gov/bills_and_notices/OIC.shtml or call FTB at (800) 338-0505.

penalty be waived due to his health problems and financial situation. It appears that appellant is arguing that his more recent difficulties provide equitable grounds to waive the penalty, rather than arguing that any health problems or other circumstances caused him to file his tax return late. However, the late-filing penalty can only be abated if the taxpayer shows that, despite the exercise of ordinary business care and prudence, he or she could not timely file the tax return due to some reasonable cause. There is no evidence that this standard is met here. Accordingly, we have no basis to reverse FTB's imposition of the penalty.

As noted above, appellant may wish to contact FTB to learn about any programs that might be able to provide assistance.

HOLDINGS

1. FTB's proposed assessment was issued within the statute of limitations.
2. Appellant is not entitled to the claimed unreimbursed employee expense deduction of $38,608.
3. Appellant is liable for the late-filing penalty.

DISPOSITION

FTB's action is sustained.

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Grant S. Thompson
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Grant S. Thompson
Administrative Law Judge

We concur:

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Tommy Leung
Administrative Law Judge

DocuSigned by:
Neil Robinson
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Neil Robinson
Administrative Law Judge