OFFICE OF TAX APPEALS

STATE OF CALIFORNIA

In the Matter of the Appeal of:	) OTA Case No. 21037349
L. INGALLS	)
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	)
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	)

OPINION

Representing the Parties:

For Appellant: L. Ingalls

For Respondent: John E. Yusin, Tax Counsel IV

For Office of Tax Appeals: Andrew Jacobson, Tax Counsel III

T. STANLEY, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) section 19045, L. Ingalls (appellant) appeals an action by respondent Franchise Tax Board (FTB) proposing an additional tax of $3,497, plus applicable interest, for the 2013 taxable year.

Appellant waived the right to an oral hearing; therefore, we decide the matter based on the written record.

ISSUE

Has appellant shown error in FTB's disallowance of claimed job expenses and certain miscellaneous deductions for the 2013 taxable year?

FACTUAL FINDINGS

1. Appellant and W. Ingalls[1] jointly filed a timely 2013 California Resident Income Tax Return. Attached to the California return was appellant's U.S. Individual Income Tax Return (Form 1040), on which appellant reported itemized deductions of $88,611, including unreimbursed employee expenses (UEE) of $70,269 and tax preparation fees of

[1] W. Ingalls did not sign the appeal letter and is, therefore, not a party to this appeal.

$39, totaling $70,308, on Schedule A. Appellant reduced the combined UEE and tax preparation fees by $2,255 (2 percent of adjusted gross income (AGI) pursuant to the requirements of Internal Revenue Code (IRC) section 67(a)) to $68,053.

2. On a Form 2106, Employee Business Expenses, appellant claimed business expenses related to appellant's employment in construction, including: (1) vehicle expenses of $41,245; (2) parking fees, tolls, and transportation expenses of $200; and (3) other business expenses of $8,075. Appellant also claimed meals and entertainment of $568. This resulted in claimed business expenses of $49,804.

3. On Form 2106, appellant reported vehicle expenses for two separate vehicles. Appellant reported that Vehicle 1 was placed in service on November 9, 2012, that it was driven 31,000 miles during 2013, 100 percent of which were business miles, and that none of the miles were for commuting or personal purposes. Appellant reported that Vehicle 2 was placed in service on May 9, 2012, that it was driven 42,000 miles during 2013, 100 percent of which were business miles, and that none of the miles were for commuting or personal purposes. Appellant calculated claimed vehicle expenses of $41,245 using the 2013 IRS standard mileage rate of 56.5 cents per mile.

4. Appellant reported that one or both vehicles were available for personal use during off-duty hours, that no other vehicle was available for personal use, and that there was written evidence to support the claimed deduction.

5. On a separate federal Form 2106-EZ, Unreimbursed Employee Business Expenses, appellant claimed business expenses of $20,465 related to W. Ingalls's work as an accountant, including: (1) vehicle expenses of $3,390 (for a third vehicle not included on Form 2106); (2) travel expense of $750; (3) other business expenses of $16,175; and (4) meals and entertainment expenses of $150. For vehicle expenses, appellant claimed a vehicle that was put into service on February 19, 2013, which incurred 6,000 business miles, 1,400 commuting miles, and 3,600 commuting miles during 2013. Appellant calculated claimed, deductible vehicle expenses of $3,390. Appellant reported that the vehicle was available for personal use during off-duty hours, that W. Ingalls did not have another vehicle available for personal use, and that there was written evidence to support the claimed deduction.

6. Appellant also completed three separate federal Forms 4562, Depreciation and Amortization (including Information on Listed Property), electing to take IRC section 179 deductions totaling $5,229 for the same vehicles listed on the federal Form 2106 and Form 2106-EZ.
7. On January 11, 2018, FTB issued a Notice of Proposed Assessment (NPA) to appellant, which revised California taxable income by $68,053 based on an "Adjustment to Itemized Deduction." The NPA imposed an additional tax due of $3,497, including an alternative minimum tax of $405, plus applicable interest. The NPA stated that FTB had earlier requested in an audit letter[2] that appellant provide substantiation for claimed job expenses and miscellaneous deductions.
8. Appellant did not respond to respondent's request for information substantiating claimed job expenses and miscellaneous deductions, and on January 15, 2021, FTB issued a Notice of Action affirming its NPA.
9. This timely appeal followed.

DISCUSSION

It is well established that a presumption of correctness attends FTB's determinations of fact and that taxpayers have the burden of proving that such determinations are erroneous. (*Appeal of Head and Feliciano*, 2020-OTA-127P.) To overcome the presumed correctness of FTB's finding as to issues of fact, taxpayers must introduce credible evidence to support their assertions, and if they do not support their assertions with such evidence, FTB's determinations must be upheld. (*Ibid*.)

Income tax deductions are a matter of legislative grace, and a taxpayer who claims a deduction has the burden of proving by competent evidence that he or she is entitled to that deduction. (*New Colonial Ice Co. v. Helvering* (1934) 292 U.S. 435, 440; *Appeal of Dandridge*, 2019-OTA-458P.) To sustain the burden of proof, a taxpayer must be able to point to an applicable deduction statute and show that he or she comes within its terms. (*Appeal of Jindal*, 2019-OTA-372P.) Unsupported assertions cannot satisfy a taxpayer's burden of proof. (*Appeal of Vardell*, 2020-OTA-190P.)

[2] A copy of this audit letter was not provided in the appeal file.

A taxpayer may deduct UEE as ordinary and necessary business expenses under R&TC section 17201, which incorporates by reference IRC section 162. IRC section 162(a) authorizes a deduction for "all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business. . . . ." (See also *Haldeman v. Franchise Tax Board*, 141 Cal.App.3d 373, 376.) By contrast, personal, living, or family expenses are generally nondeductible. (IRC, § 262.) [3] The expenses must be ordinary and necessary business expenditures directly related to the taxpayer's trade or business. (IRC, § 162(a); Treas. Reg. § 1.162-1(a); *Appeal of La Rosa Capital Resource, Inc.*, 2020-OTA-220P.)

Performing services as an employee constitutes a trade or business. (*Richards v. Commissioner*, T.C. Memo. 2014-88.) However, an expense is not "necessary," as that term is used in IRC section 162, when an employee has a right to reimbursement for expenditures related to his or her status as an employee but fails to claim such reimbursement. (*Orvis v. Commissioner* (9th Cir. 1986) 788 F.2d 1406, 1408.) The taxpayer bears the burden of proving that he or she is not entitled to reimbursement from her employer for such expenses. (See *Fountain v. Commissioner* (1973) 59 T.C. 696, 708.)

IRC section 274(d),[4] prohibited an IRC section 162(a) deduction for the following types of expenses unless they were substantiated by adequate records or by sufficient evidence corroborating the taxpayer's own statement: (1) any travel expense, including meals and lodging away from home; (2) any item with respect to an activity in the nature of entertainment, amusement, or recreation; (3) an expense for gifts; or (4) the use of "listed property," as defined in IRC section 280F(d)(4), which includes passenger automobiles. (See *Roberts v. Commissioner*, T.C. Memo. 2012-197.) To qualify for a deduction, the taxpayer must meet heightened requirements to substantiate a claimed expense with adequate records or sufficient evidence to corroborate the taxpayer's own statement as to: (1) the amount of the expense or other item; (2) the time and place of the travel, entertainment, amusement, recreation, or use of the property, or the date and description of the gift; (3) the business purpose of the expense or other item; and (4) the business relationship to the taxpayer of the persons entertained or

[3] IRC sections 162 and 262 are generally incorporated into California law by R&TC section 17201

[4] R&TC section 17201 incorporates IRC section 274 into California law. All references to IRC section 274(d) are to the version in effect during the 2013 tax year.

receiving the gift. (IRC, § 274(d).)[5] "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 v. Commissioner*, T.C. Memo. 2010-60.) Federal regulations provide that taxpayers have maintained "adequate records" if they keep a contemporaneous log or diary, combined with supporting documents, which substantiate the required elements of the expense, such as the amount, the date, and the 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 or her own statement containing specific detail as to each element, and "other corroborative evidence sufficient to establish such element." (Treas. Reg. § 1.274-5T(c)(3).)

In the present appeal, FTB denied $68,053 out of total California itemized deductions of $84,691 that appellant and W. Ingalls claimed on their 2013 California return. This amount represents the entirety of the UEE deductions claimed on appellant's federal Schedule A. At protest and on appeal, appellant asserts that FTB should have requested supporting documents sooner, and that the records were stored on a computer that is no longer available to him. Appellant claims "I did nothing wrong . . ." and "2013 is so far back I can't even find any info from that year[.] I have no records."

Vehicle Mileage

Vehicle mileage deductions are subject to the heightened substantiation requirements of IRC section 274. Appellant was not able to provide any records and therefore failed to substantiate the claimed deductions for three vehicles. Moreover, appellant has not provided evidence such as employer reimbursement policies, requests for reimbursement, and employer correspondence to show that this claimed mileage was not reimbursed by appellant's or W. Ingalls' employers. Therefore, appellant has failed to meet his burden of proving that the claimed vehicle mileage was necessary for appellant's trade or business, or for W. Ingalls' employment. (*Orvis v. Commissioner*, *supra*, 788 F.2d at p. 1408.) Thus, appellant has failed to show error in FTB's disallowance of claimed mileage.

[5] The version of the statute that applies to the taxable year at issue.

IRC Section 179[6] Immediate Deduction of Depreciation Expenses

IRC section 167(a) allows a deduction for a reasonable allowance for the exhaustion, wear and tear for property used in the trade or business, or for property held for the production of income. Alternatively, a taxpayer may deduct as an expense the cost of qualifying property under IRC section 179, rather than choosing to recover such costs through depreciation deductions. "A taxpayer may elect to treat the cost of any [IRC] section 179 property as an expense which is not chargeable to capital account." (IRC, § 179(a).) "Any cost so treated shall be allowed as a deduction for the taxable year in which the [IRC] section 179 property is placed in service." (*Ibid*.) IRC section 179 property is defined, in relevant part, as property: (A) which is tangible property (to which IRC section 168 applies); (B) which is [IRC] section 1245 property[7]; and (C) "which is acquired by purchase for use in the active conduct of a trade or business." (IRC, § 179(d)(1).) However, "[a]ny employee use of listed property shall not be treated as use in a trade or business for purposes of determining the amount of any depreciation deduction allowable to the employee (or the amount of any deduction allowable to the employee for rentals or other payments under a lease of listed property) *unless such use is for the convenience of the employer and required as a condition of employment*." (IRC, § 280F(d)(3)(A), italics added.) Employee use means "any use in connection with the performance of services as an employee." (IRC, § 280F(d)(3)(B).)[8]

Despite completing three federal Forms 4562, appellant and W. Ingalls did not claim an IRC section 179 deduction on their 2013 California return. Rather, they reported employee business expenses on Forms 2106 and 2106-EZ, equaling the UEE listed on Schedule A. These amounts ultimately formed part of the California itemized deductions that were denied by FTB. Nevertheless, because depreciation and other actual expenses, including an IRC section 179 deduction, may be claimed as a deduction in place of vehicle mileage, we examine whether appellant would qualify for an IRC section 179 deduction.

For the deduction to apply, appellant must prove that he and W. Ingalls used the three

[6] IRC sections 167 and 179 are incorporated into California law by R&TC section 17201.

[7] As relevant to this appeal, "'[IRC] section 1245 property' means any property which is or has been property of a character subject to the allowance for depreciation provided in [IRC] section 167 and is personal property." (IRC, § 1245(a)(3)(A).)

[8] The limitation of IRC section 280F(d)(3)(A) applies to IRC section 179 deductions. (IRC, § 280F(d)(1).)

vehicles for the convenience of their employers and that such use was required as a condition of their employment. (IRC, § 280F(d)(1) & (3)(A).) Appellant has provided no evidence to this effect, and he admits that he does not possess any such evidence. Therefore, appellant has failed to show that the vehicles were acquired for use in the active conduct of a trade or business. Additionally, appellant has failed to provide documentation that support the acquisition cost of the vehicles, or that otherwise support the total claimed IRC section 179 deductions of $5,229. (See Treas. Reg. 1.6001-1(a).) Finally, the two vehicles that were placed into service in 2012 do not qualify for an IRC section 179 deduction in 2013, because appellant was required to claim this deduction during the 2012 tax year. (IRC § 179(a).)

Therefore, we find that appellant and W. Ingalls do not qualify for a 2013 IRC section 179 deduction in place of their denied vehicle mileage.

Parking Fees, Tolls, and Transportation Expenses

As previously noted, personal, living, or family expenses are generally nondeductible pursuant to IRC section 162(a). (IRC, § 262.) "Moreover, expenses that a taxpayer generally incurs in commuting between his home and his place of business are personal and nondeductible." *Burger v. Commissioner*, T.C. Memo. 2021-89; see also Treas. Reg. § 1.262-1(b)(5).)

On appellant's federal Form 2106*,* appellant claimed parking fees, tolls, and transportation expenses of $200. Appellant has not argued, and there is no evidence to show, that the claimed parking fees, tolls, and transportation expenses were not commuting expenses, or that they fell within a recognized exception. Therefore, appellant has failed to meet his burden of showing that claimed parking fees, tolls, and transportation expenses were anything other than nondeductible personal expenses. (IRC, § 262.)

Traveling Expenses

Taxpayers may deduct all ordinary and necessary traveling expenses (including amounts expended for meals and lodging other than amounts which are lavish or extravagant under the circumstances) while away from home in the pursuit of a trade or business. (IRC, § 162(a)(2).) Unreimbursed traveling expenses, such as hotels and parking, are entitled to be deducted as business expenses if they "are reasonable and necessary in the conduct of the taxpayer's business and directly attributable to it. . . ." (Treas. Reg. § 1.162-2(a).) As discussed above, IRC section 274(d) requires that taxpayers satisfy the heightened requirements to substantiate various expenses, including travel, meal, and entertainment expenses, with "adequate records" showing the amount of the expense, the time and place of the expense, the business purpose for the expense, and the business relationship to the taxpayer of the person receiving the benefit. (See also Treas. Reg. § 1.274-5T(b)(2).)

Appellant has failed to provide copies of the reimbursement policies for W. Ingalls' two employers. Appellant has likewise failed to provide records showing whether W. Ingalls requested reimbursement under any of these policies and whether she received any responses from those employers. Therefore, appellant has failed to prove that W. Ingalls' travel expenses were necessary pursuant to IRC section 162(a). Likewise, appellant concedes that he has no records such as receipts or a contemporaneous log for 2013. Therefore, appellant has failed to substantiate W. Ingalls' claimed 2013 travel expenses. Thus, appellant has failed to show error in FTB's disallowance of W. Ingalls' claimed travel expenses.

Business Meal Expenses

Unreimbursed business meal expenses are deductible when incurred if directly connected with a taxpayer's trade or business. (IRC, §§ 162(a) and 274(a).) Such expenses are subject to the heightened substantiation requirements of IRC section 274. In addition, a business meal deduction will generally not be allowed for the unreimbursed expense of any food or beverages if the expense is "lavish or extravagant under the circumstances," or the taxpayer is not present when such food and beverages is furnished. (IRC, § 274(k)(1).)

Adequate records must be prepared and maintained for each element of a claimed meal expense "at or near the time of the expenditure or use." (Treas. Reg. § 1.274-5T(c)(2)(ii)(A).) In the alternative, each element of a claimed meal expense deduction may be established by the

taxpayer's own written or oral statements that contain "specific information in detail as to such element," and "by other corroborating evidence sufficient to establish such element." (Treas. Reg. § 1.274-5T(c)(3)(i).)

In the absence of employer reimbursement policies, requests for reimbursement and employer responses, appellant has not met his burden of proving that the claimed expenses were not reimbursed or subject to reimbursement. Appellant has also failed to substantiate claimed meal expenses were incurred. Appellant has provided neither contemporaneous meal schedules, nor retrospective lists that support the deductions. Thus, appellant has failed to show error in FTB's disallowance of business meal expenses.

Other Business Expenses

Appellant has provided no list itemizing the specific trade or business expenses that are included in the claimed amounts, nor has he provided any evidence showing that the claimed expenses were incurred pursuant to an employer's trade or business. Therefore, appellant has failed to show that claimed other business expenses for 2013 were ordinary and necessary or that they were incurred while carrying on an employer's trade or business.

HOLDING

Appellant has failed to show error in FTB's disallowance of claimed job expenses and certain miscellaneous deductions for the 2013 taxable year.

DISPOSITION

FTB's action is sustained.

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Teresa A. Stanley
Administrative Law Judge

We concur:

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Administrative Law Judge

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Andrea L.H. Long
Administrative Law Judge

Date Issued: 11/22/2021