87-SBE-055

BEFORE THE STATE BOARD OF EQUALIZATION

OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
) No. 84A-1000-VN
PETER J. AND SANDRA S. GELMINI)

Appearances:

For Appellant: Sandra S. Gelmini
in pro per.

For Respondent: Michael R. Kelly
Counsel

O P I N I O N

This appeal is made pursuant to section 18593[1/] of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protest of Peter J. and Sandra S. Gelmini against proposed assessments of additional personal income tax in the amounts of $114.15, $307.00, and $309.00 for the years 1978, 1979, and 1980, respectively.

1/ Unless otherwise specified, all section references are to sections of the Revenue and Taxation Code as in effect for the years in issue.

Appeal of Peter J. and Sandra S. Gelmini

The question presented for our decision is whether appellants are entitled to travel and entertainment expense deductions claimed in 1978 and 1979 and educational expense deductions claimed in 1980.

In 1978, Peter J. and Sandra S. Gelmini, husband and wife, started a travel agency in Hacienda Heights with another married couple. Called "A Premier Travel Service," the business was first organized as a partnership, but appellants purchased the partnership interest of the other couple in May 1980 and, thereafter, operated the business as their sole proprietorship. During the appeal years, Mrs. Gelmini, who had prior experience as a travel agent, apparently managed the travel agency. During part of the first year, 1978, she was also employed by another travel agency from which she received $4,997 in commissions. Mr. Gelmini had a full-time job with AMF Voit, Inc., but allegedly volunteered his services to the agency in his spare time. Two of appellant's daughters were also employed by the office as part-time travel agents.

For 1978 and 1979, appellants filed forms schedule C (Profit or (Loss) from Business or Profession) and claimed travel and entertainment expense deductions for alleged "familiarization trips" taken by them to various vacation spots. In the travel business, it is common for airlines, resorts, and others in the trade to promote their tour packages by offering familiarization trips to travel agents at discounted prices. These trips allow agents to gain firsthand knowledge of the accommodations, facilities, transportation, services, and activities offered at tourist areas, which enable them to sell available tour packages to their customers, (See Leamy v. Commissioner, 85 T.C. 798 (1985).) In 1978 and 1979, appellants visited such places as San Jose, Las Vegas, New Orleans, Florida, New England, and Europe. Appellants' five children accompanied them on some of these trips. For 1980, appellants claimed similar travel and entertainment expense deductions for various tours, including Austria and Hawaii. In addition, they claimed educational expense deductions for traveling and, allegedly, attending seminars and conferences in such locales as San Diego, the Orient, and Hawaii.

During the subsequent audit, appellant provided respondent with written chronological summaries of their many excursions as well as cancelled checks and invoices to show the related transportation, hotel, and food

costs. However, apparently because appellants' schedules C for 1978 and 1979 did not indicate that they were in the travel business nor show any income therefrom, respondent assumed that the travel and entertainment expenses were incurred in connection with Mrs. Gelmini's employment at the other travel agency. Consequently, respondent treated these expenses as largely personal expenses and disallowed 80 percent of the travel and entertainment expense deductions claimed in these two years. For 1980, the Franchise Tax Board determined appellants were operating a travel agency since they reported gross receipts of $450,741 and thus allowed all of their travei and entertainment expense deductions. On the other hand, respondent disallowed $3,572 of their claimed $4,209 educational expense deductions in 1980 for failure to substantiate a business purpose.

It is well settled that deductions are a matter of legislative grace and that the burden is on the taxpayer to show by-competent evidence that he is entitled to the deductions claimed. (New Colonial Ice Co. v. Helvering, 292 U.S. 435 [78 L.Ed. 1348] (1934).) First, section 17202, subdivision (a), which is substantially similar to Internal Revenue Code section 162(a), allows as a deduction all ordinary and necessary expenses paid or incurred by the taxpayer in carrying on any trade or business. Traveling expenses are deductible only if the trip is related primarily to the taxpayer's trade or business; expenses attributable to a spouse and children accompanying the taxpayer on a business trip are deductible only if it is adequately shown that their presence had a bona fide business purpose. (Treas. Reg. § 1.162-2.) A deduction for any traveling or entertainment expense will not be allowed unless substantiated by adequate records or sufficient evidence corroborating the taxpayer's own statement. (Rev. & Tax. Code, § 17296; Appeal of Bruce D. and Donna G. Varner, Cal. St. Bd. of Equal., July 26, 1978.)

At the hearing on this matter, the Franchise Tax Board stated that it treated appellants' travel and entertainment deductions for 1978 and 1979 differently than the deductions for 19.80. Since appellants' schedules C for 1978-79 showed no income from a travel agency and Mrs. Gelmini received income from the travel agency where she was employed, respondent's audit staff was under the impression that appellants did not start their travel agency until 1980 when they reported gross receipts or sales of $450,741 on a schedule C for that

year. Moreover, because appellants had apparently failed to file partnership returns for the first two appeal years, respondent was not aware that the travel agency was operated as a partnership during that time.

'In response, Mrs. Gelmini testified that the business was started in 1978 as a partnership. After this board granted Mrs. Gelmini more time to file additional information, appellants submitted unsigned partnership returns for 1978 and 1979 which showed that the partnership began operating the travel agency in 1978 and derived gross receipts or sales of $38,878 in 1978 and $684,859 in 1979. Appellants further explained that in 1978 and 1979 they were required to pay various costs of the travel agency, including the travel and entertainment expenses at issue, to keep the business afloat. The other partners agreed that these costs would be allocated to appellants who then claimed the expenses as business deductions on the schedules C of their personal tax returns for 1978 and 1979.[2]

In this case, we find no material differences between the travel and entertainment deductions for 1978 and 1979 and those for 1980. The travel summaries that appellants submitted to verify their expenses and itineraries show that the deductions are essentially the same for each of the appeal years. Respondent disallowed 80 percent of the deductions in 1978 and 1979 based on the assumption that appellants were not operating an independent travel agency until 1980. While appellants may have contributed to that impression by failing to indicate their gross receipts from their travel agency in the first two years, the fact of the matter is that appellants were operating the business in.1978 and 1979. Since respondent allowed the same deductions in 1980, it appears that appellants should be entitled to some of the travel and entertainment expense deductions claimed in 1978 and 1979. However, the evidence also shows that appellants claimed deductions for trips taken by the whole family when only Mrs. Gelmini and the two daughters worked at the travel agency. Appellants contend that Mr. Gelmini's presence on these familiarization trips afforded a man's view and that often their three children were required to attend to help evaluate "family loca-

2/ Since it is not necessary to do so, neither party having raised the issue, we make no decision regarding the propriety or impropriety of appellants' allocation of the expenses of the partnership to themselves.

tions." (App. Br. at 2-3.) However, appellants have admitted that all of their children accompanied them on some of these excursions because they could not find any babysitters to watch them at home. Appellants' showing that they incurred travel expenses is insufficient without proof that all of these expenditures had a business purpose. (Appeal of Harold and Jean Goldman, Cal. St. Bd. of Equal., Dec. 3, 1985.) Based on the absence' of any evidence demonstrating that the presence of all family members were needed for bona fide business purposes, we must conclude that appellants are entitled to only SO percent of their claimed travel and entertainment expense deductions for 1978 and 1979.

Second, educational expenditures are deductible as ordinary and necessary business expenses if the education was undertaken primarily either (1) to maintain or improve skills needed by the taxpayer in his employment or business, or (2) to meet the employer's requirements, applicable law, or regulations imposed as a condition for the taxpayer's retention of his employment, status, or salary. (Treas. Reg. § 1.162-5(a).) Expenditures for travel as a form of education are deductible only if the travel is directly related to the duties of the taxpayer in his employment, (Appeal of Lawrence D. and Barbara L. Parker, Cal. St. Bd. of Equal., Sept. 10, 1985.)

With regard to the disallowed educational expense deductions for 1980, appellants have merely contended that travel is a necessary educational expense of a travel agency. However, educational travel is considered primarily personal in nature, and therefore, nondeductible, unless shown to improve skills needed by the taxpayer in his employment or business. (Appeal of Bernice V. Grosso, Cal. St. Bd. of Equal., Aug. 1, 1980.) Appellants have not presented any evidence to show how the travel expenses that were disallowed as educational deductions improved their skills in operating their travel agency. Since appellants have not met their burden of substantiating the business purpose of all of the educational expense deductions claimed in 1980, we must conclude that appellants were not entitled to deductions in an amount greater than that allowed by respondent.

Based on the'foregoing, we find that respondent's action in this matter for 1978 and 1979 must be modified but that its action for 1980 must be upheld.

Appeal of Peter J. and Sandra S. Gelmini

ORDER

Pursuant to the views expressed in the opinion of the board on file in this proceeding, and good cause appearing therefor,

IT IS HEREBY ORDERED, ADJUDGED AND DECREED, pursuant to section 18595 of the Revenue and Taxation Code, that the action of the Franchise Tax Board on the protest of Peter J. and Sandra S. Gelmini against proposed assessments of additional personal income tax in the amounts of $114.15, $307.00, and $309.00 for the years 1978, 1979, and 1980, respectively, be and the same is hereby modified with respect to the assessments for 1978 and 1979. In all other respects, the action of the Franchise Tax Board is sustained.

Done at Sacramento, California, this 28th day Of July , 1987, by the State Board of Equalization, with Board Members Mr. Collis, Mr. Bennett, Mr. Carpenter and Ms. Baker present.

Conway H. Collis, Chairman

William M. Bennett, Member

Paul Carpenter, Member

Anne Baker*, Member

________________, Member

*For Gray Davis, per Government Code section 7.9