Vehicle Expenses Denied

This case is shows the kind of information some taxpayers produce when the audit hits. Hopefully none of your clients have records like this taxpayer. Maybe sharing this case with them will help them keep good records.

Katrina Taylor was an employee as well as a self-employed individual. Her MFJ tax return for the year reported her wages of $96,000 for working full time at a hospital. It also included a Schedule C for a long-term care billing business.

The Schedule C includes gross income for the year of $0. The expenses for the activity came to about $76,000, almost all of which was vehicle related expenses. The returns showed results of $5,891 of the Earned Income Tax Credit and $2,665 of refundable child tax credit.

IRS denied the vehicle expenses claiming the expenses were not properly substantiated. Further IRS stated if the expenses had been substantiated, they would have been start-up expenses. IRS also assessed the accuracy related penalty. Off to Tax Court the case went.

Tax Court agreed with IRS denying the expenses and assessing the penalty. Mrs. Taylor testified she had created spreadsheets shortly before the audit and based the spreadsheet on notes but she did not produce the notes. Tax Court felt the spreadsheets were not credible and it was clear they were not prepared contemporaneously at the time the expenses were incurred. Some issues Tax Court found include:

1) The return's Form 4562 showed two vehicles, both used 100% for business use. The taxpayer's testimony showed four vehicles, all of which were less than 100% business use.

2) At audit Mrs. Taylor produced a spreadsheet showing four vehicles. The TOTAL miles for the four vehicles came up to the same TOTAL miles on the return for the two vehicles show on the return. Each entry on her spreadsheet showed the date, time, destination, and beginning and ending odometer readings. Various entries had ENDING odometer readings that were higher than the BEGINNING odometer readings.

4) Each entry had "Distribution information brochure/market" as the description of the activity performed. Mrs. Taylor testified she made these trips to distribute a one-page brochure of the services she was offering. Tax Court felt this identical description on EVERY entry was not sufficient detail to substantiate the trips.

5) None of the entries on the spreadsheet identified the time she spent at the destination or the specific activity she performed while there.

5) Some entries appeared to be inflated such as one day's entry that said 1,696 miles which would require traveling for 24 consecutive hours a day at an average of 70 miles per hour with NO stops for client meetings, rest stops, fuel, etc.

6) Some entries showed differing miles for the same destination, such as two entries to Charleston, SC that showed 1,382 and 1,583 miles. Mrs. Taylor was unable to explain the differences.

7) There were 144 full-day trips. Tax Court felt Mrs. Taylor was not reasonably able to make these trips while also working full time at her job at a hospital.

8) There were several trips to the same area in the same month and Mrs. Taylor was unable to provide a reason as to why the trips weren't set up to visit multiple prospective clients on the same trip.

When all issues of concern were looked at the Tax Court felt the spreadsheet was not reliable and agreed with IRS in denying the Schedule C loss and assessing the accuracy related penalty.

Katrina E. & Avery Taylor, TC Memo 2017-99. This case can be found by going to www.ustaxcourt.gov, clicking on Opinion Search and entering Taylor in the Case Name box.

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