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Auto expenses are a very common deduction for business owners and employees who must travel. Often the taxpayer does not know the exact amounts necessary to calculate the proper deduction and the tax preparer must estimate the mileage, business percentage, and ultimate auto deduction with the client's help. Tax preparers should remind their clients to have proper substantiation or, if the IRS examines the return, the deduction will more than likely be denied.

If the substantiation is lost or stolen, the IRS will generally deny the deduction because the *Cohan* rule (which allows a court to estimate deductible amounts of unsubstantiated expenses) cannot be applied for certain expenses, including automobile expenses (Sec. 274(d)(4)). In the case of a lost or stolen substantiation, combined with the nonavailability of contemporaneous records, substitute records may be provided, but they must include sufficient information to support the deduction (Temp. Regs. Sec. 1.274-5T(c)).

On September 24, 2008, the Tax Court, in a summary decision, upheld the Service's disallowance of an auto expense deduction of a traveling salesperson due to lack of substantiation (*Niyitegyeka*, T.C. Summ. 2008-129). It was obvious that the taxpayer traveled for business and would ordinarily be entitled to a deduction, but the submitted evidence was too weak to allow it.

Background

Sec. 6001 requires taxpayers to keep records to substantiate their tax liability. In the absence of such evidence, expenses can be estimated using circumstantial evidence per *Cohan*, 39 F.2d 540 (2d Cir. 1930). However, Sec. 274(d) overrides the *Cohan* rule and requires a taxpayer to substantiate auto expenses (along with a few others).

Temp. Regs. Sec. 1.274-5T(c)(2) expands upon the substantiation rule. The regulation states, "An account book, diary, log, statement of expense, trip sheet, or similar record must be prepared or maintained in such manner that each recording of an element of an expenditure or use is made at or near the time of the expenditure or use." This means the record does not have to be documented at the exact same time as the expense, but it must be done within a reasonable time so that the time, place, amount, and business purpose can be recorded. The regulation gives the example that maintaining a log on a weekly basis is near enough to the expenditure to count as proper substantiation. The evidence may be written or recorded on an accessible computer memory device. The taxpayer may omit certain confidential information from the records as long as the information is available upon request.

Niyitegyeka

In *Niyitegyeka*, the taxpayer was a traveling salesperson in training. He would go to his employer's office in Manhattan and then drive to his customers' locations. The employer's policy was to not reimburse trainees for expenses related to this type of travel, including hotels, meals, and mileage. The taxpayer traveled often and went as far as Queens, New Jersey, and Connecticut. These facts were not in dispute.

Because the travel was definitely for business and the expenses were not reimbursable, a deduction for business mileage was proper. However, upon examination, the taxpayer did not present any evidence to substantiate the mileage. Thus, the Service disallowed the deduction. The taxpayer claimed that he kept his records in his car, which had been stolen. The taxpayer filed a police report and the car was later recovered, but the business records were gone.

The Tax Court gave the taxpayer the opportunity to present other evidence besides a contemporaneous log or receipts. Accordingly, the taxpayer presented a computer listing, purportedly from the employer, that detailed the dates, names, and amounts of his draw and commission activities.

According to the Tax Court judge who heard the case, this evidence was insufficient to justify granting the deduction, and the IRS's decision to deny the deduction was upheld. Specifically, the judge took issue with the following:

This evidence was being presented for the first time at trial, as opposed to being available for the examiner.

The listing was on plain white paper, which had no identifying marks, letterhead, or other indication of its source.

No one from the employer was presented to corroborate the listing.

There were no addresses, locations, or distances listed, so mileage could not be determined.

Neither the tax preparer, the taxpayer's clients, nor anyone else was called by the taxpayer to testify on his behalf.

Accordingly, the court found that the listing was not sufficient evidence to support the deduction that the taxpayer sought. The judge noted that no evidence presented in this case provided "a rational basis on which we may determine even a partial deduction."

Conclusion

In the *Niyitegyeka* case, because it was an undisputed fact that deductible travel did happen, it seems that had the taxpayer done a bit more work there might have been sufficient substantiation for the Tax Court to approve the deduction. Tax preparers can provide a great service by being sure their clients have proper documentation for automobile expenses in case of an audit. This may seem daunting to the client, so the tax preparer can be the client's friend by knowing how the client goes about his or her business and suggesting a method that is easy for the taxpayer to use. Does the client have an appointment book in which the business mileage for each appointment could be written down? If not, can the client use a wall calendar to document the business mileage?

Keeping track of expenses on a regular basis can be an annoying chore. However, the bottom line is that a simple process of documenting a few extra items, using tools the client already has, can save the client a big headache during an examination.

EditorNotes

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