13-1292
TAX TYPE: INCOME TAX
TAX YEARS: 2005 through 2011
DATE SIGNED: 12-3-2015
COMMISSIONERS: M. CRAGUN, R. PERO, R. ROCKWELL
RECUSED: J. VALENTINE
GUIDING DECISION

BEFORE THE UTAH STATE TAX COMMISSION

TAXPAYER-1, & TAXPAYER-2,[1] Petitioner, v. AUDITING DIVISION OF THE UTAH STATE TAX COMMISSION, Respondent.	**FINDINGS OF FACT, CONCLUSIONS OF LAW, AND FINAL DECISION** Appeal No. 13-1292 Account No. ##### Tax Type: Income Tax Years: 2005, 2006, 2007, 2008, 2009, 2010 & 2011 Judge: Chapman

Presiding:
Robert P. Pero, Commissioner
Kerry R. Chapman, Administrative Law Judge

Appearances:
For Petitioner: TAXPAYER-1, Taxpayer
REPRESENTATIVE FOR TAXPAYER'S, Accountant
For Respondent: REPRESENTATIVE FOR RESPONDENT, Assistant Attorney General
RESPONDENT, from Auditing Division

STATEMENT OF THE CASE

TAXPAYER-1 ("Petitioner" or "taxpayer") is appealing individual income tax assessments imposed by Auditing Division ("Respondent" or "Division"). This matter came before the Utah State Tax Commission for a Formal Hearing on August 11, 2015. Based upon the evidence and testimony, the Tax Commission hereby makes its:

1 The Division issued its 2005, 2008, and 2009 assessments to TAXPAYER-1 only, while it issued its 2006, 2007, 2010, and 2011 assessments to both TAXPAYER-1 and his wife, TAXPAYER-2. For all years at issue, TAXPAYER-1 and his wife submitted joint returns. For ease of reference, only TAXPAYER-1 will be referred to as the "Petitioner" or "taxpayer" in the remainder of this decision.

FINDINGS OF FACT

1. The tax at issue is individual income tax.

2. The tax years at issue are 2005, 2006, 2007, 2008, 2009, 2010, and 2011.

3. On April 18, 2013, the Division issued Notices of Deficiency and Estimated Income Tax ("Statutory Notices") for the seven years at issue,[2] in which it imposed additional tax, 10% penalties for failure to timely file, 10% penalties for failure to timely pay, and interest (calculated as of March 31, 2013),[3] as follows:

Year	Tax	Penalties	Interest	Total
2005	$$$$$	$$$$$	$$$$$	$$$$$
2006	$$$$$	$$$$$	$$$$$	$$$$$
2007	$$$$$	$$$$$	$$$$$	$$$$$
2008	$$$$$	$$$$$	$$$$$	$$$$$
2009	$$$$$	$$$$$	$$$$$	$$$$$
2010	$$$$$	$$$$$	$$$$$	$$$$$
2011	$$$$$	$$$$$	$$$$$	$$$$$

4. The Commission held an Initial Hearing in this matter and issued its Initial Hearing Order on August 25, 2014. The taxpayer requested to proceed to a Formal Hearing.

5. As already mentioned, the Division submitted the Utah resident individual income tax returns that the taxpayer filed for 2005, 2006, 2007, 2009, 2010, and 2011 tax years. For these same years, the Division also submitted the federal returns that the taxpayer had filed with the Internal Revenue Service ("IRS") or the IRS transcripts for the taxpayer's account.[4] The taxpayer's Utah returns reflect the same

2 Respondent's Formal Hearing Exhibits #1 (2005), #5 (2006), #8 (2007), #11 (2009), #14 (2010), and #17 (2011) ("Exhibits R-1, R-5, R-8, R-11, R-14, and R-17"). At the Formal Hearing, the Division did not submit as evidence a copy of the Statutory Notice it issued for the 2008 tax year, presumably because the taxpayer is not contesting any of portion of the 2008 assessment at the Formal Hearing. The Division, however, included a copy of the 2008 Statutory Notice with the Answer to Petition for Redetermination that it submitted in June 2013.

3 Interest continues to accrue until any tax liability is paid.

4 Exhibits R-3 (2005), R-7 (2006), R-10 (2007), R-13 (2009), R-16 (2010), and R-19 (2011).

amounts of federal adjusted gross income ("FAGI") and itemized deductions that the taxpayer reported to the IRS.

6. Even though the amounts the taxpayer reported on his Utah returns match the amounts he reported on his federal returns, the Division determined that a number of changes needed to be made to the income, expenses, and deductions he had reported to both agencies. The taxpayer contests some of the items that the Division changed, but does not contest some of the items that it changed. Nevertheless, for those changes the taxpayer is contesting, he indicates that the Tax Commission should not have made the changes because the IRS has not challenged these items. In addition, for those items the taxpayer is contesting at the Formal Hearing (as detailed later in the decision), he contends that he has submitted sufficient evidence to show that the Division's changes are improper and should be reversed.

7. The Division asserts that it has the right to adjust the income, expenses, and deductions the taxpayer claimed for federal and state tax purposes even if the IRS did accept the taxpayer's federal returns and has not audited them or made similar adjustments. The Division also asked the Commission to consider that in 2008, TAXPAYER-1 was convicted of two felonies for tax evasion and a misdemeanor for attempted tax evasion in regards to his Utah income tax liability for the 2001 through 2004 tax years.[5] As a result, the Division claims that TAXPAYER-1's credibility is a concern, which has required it to examine whether the items he reported on his 2005 through 2011 federal and Utah tax returns are correct. The Division allowed a number of the items TAXPAYER-1 reported on his 2005 through 2011 tax returns. However, the Division assessed those items for which it determined that TAXPAYER-1's tax records were insufficient to support a specific item of income, expense, or deduction. The Division referred the Commission to Utah Admin. Rule R865-9I-18 ("Rule 18"), which provides that a taxpayer should preserve records of all transactions affecting

5 Exhibit R-20, p. 53.

income or expense, or gain or loss, and of all transactions for which deductions may be claimed and make the records available to an authorized agent of the Tax Commission when requested, for review or audit.

8. In addition, for those assessment items that the taxpayer is contesting, the Division relies on the taxpayer not meeting his burden of proof to show that the assessments are incorrect. The Division contends that the evidence submitted by the taxpayer at the Formal Hearing is insufficient to show that it has incorrectly assessed any of the contested items.

9. At the Formal Hearing, the taxpayer is contesting seven of the eight issues he had previously contested at the Initial Hearing. The taxpayer also asked the Commission to consider a new issue at the Formal Hearing that he had not raised at the Initial Hearing. For purposes of conducting the Formal Hearing, the issues were addressed in the same order as they had been discussed in the Initial Hearing Order. As a result, the Commission will address the issues in that same order for purposes of this Formal Hearing decision.

Issue 1: Income from Cancellation of Debt – 2005 Tax Year

10. For the 2005 tax year, the Division assessed tax on $$$$$ of debt cancellation income for which the taxpayer had claimed an exclusion from taxation.[6] This is the only item on the Division's 2005 assessment that the taxpayer is contesting. On his 2005 federal return, the taxpayer claimed that he qualified to exclude the $$$$$ of debt cancellation income from taxation because he was insolvent.[7] Both parties agree that a party who is insolvent may qualify to exclude debt cancellation income under Internal Revenue Code ("IRC") §108.

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6 Exhibit R-1.

7 On the taxpayer's 2005 federal tax return, the taxpayer wrote "SEE STATEMENT" on line 21 (Other income) and entered $0. Exhibit R-3. The taxpayer contends that in the "statement" he attached to his federal return, he indicated that the $$$$$ of cancelled debt income was excluded from gross income because he was insolvent. The Division stated that it does not have a copy of any "statement" that TAXPAYER-1 provided with his 2005 federal return, and TAXPAYER-1 did not provide a copy of the "statement" to the Commission. To show that TAXPAYER-1 also excluded the $$$$$ of cancelled debt income from his Utah taxable income, the Division showed that the taxpayer's 2005 Utah return reflects the same $$$$$ amount of federal adjusted gross income ("FAGI") as reflected on his 2005 federal return.

11. To show that he was insolvent, TAXPAYER-1 provided a copy of a "Balance Sheet of TAXPAYER-1 & TAXPAYER-2" ("Balance Sheet") showing that he had a negative net worth as of December 31, 2005, the last day of the 2005 tax year. On the Balance Sheet, TAXPAYER-1 attested that as of December 31, 2005, his total assets amounted to $$$$$ and that his total liabilities amounted to $$$$$, resulting in a net worth of negative $$$$$.[8] TAXPAYER-1 stated that he provided this information to the IRS to show that he qualified for the exception from taxation on the $$$$$ of cancellation debt income.

12. The Division admits that the IRS accepted the taxpayer's 2005 federal return and has not audited TAXPAYER-1's claim that he qualified for an exception from taxation on the cancelled debt. The Division, however, asks the Commission to sustain its disallowance of the exclusion from income that TAXPAYER-1 claimed and to find that the $$$$$ of debt cancellation is income subject to taxation. The Division makes several arguments to support its position.

13. First, the Division points out that IRC §108(a)(1)(B) provides that debt cancellation income is excluded from taxation if the cancellation or discharge "occurs when the taxpayer is insolvent." IRC §108(d)(3) further indicates that the taxpayer's insolvency is to "be determined on the basis of the taxpayer's assets and liabilities immediately before the discharge." The Division states that because the taxpayer has not shown the date on which the $$$$$ of debt was discharged or cancelled, he has not shown that a balance sheet showing his assets and liabilities as of December 31, 2005 necessarily complies with the federal law. The Division's position is well taken. If the taxpayer's Balance Sheet shows his net worth "immediately before the discharge," it would appear that the entity that cancelled the debt would have had to cancel it either on December 31, 2005 or on January 1, 2006. If the latter, the debt cancellation income would have been a 2006, not a 2005, tax matter. Regardless, without evidence of the date on which the debt was cancelled, the taxpayer

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8 Petitioner's Exhibit #1 ("Exhibit P-1").

has not shown that a December 31, 2005 Balance Sheet shows him to be insolvent "immediately before the discharge."

14. Second, the Division points out that TAXPAYER-1 did not submit to the IRS a Form 982 (Reduction of Tax Attributes Due to Discharge of Indebtedness (and Section 1082 Basis Adjustment)).[9] Form 982 indicates that "[t]axpayers who exclude discharge of indebtedness income from gross income generally, must reduce certain tax attributes either dollar for dollar or 33 cents per dollar" and provides a method for a taxpayer who claims an exclusion from taxation for debt cancellation income to report the applicable reduction in basis.[10] The taxpayer has provided no information to show that he has reduced his tax attributes by the applicable amount of the debt cancellation or to show that he was not required to reduce his tax attributes.

15. Third, the Division questions whether TAXPAYER-1 has properly reported all of his assets on the December 31, 2005 Balance Sheet. The Division points out that TAXPAYER-1 did not list any checking or savings accounts, any retirement funds, any stocks and bonds, or other similar assets on his Balance Sheet. The Division indicates that it found a checking account in TAXPAYER-1's name that had a balance of $$$$$ as of the December 31, 2005 date of the Balance Sheet. TAXPAYER-1 agreed that he should have listed this asset on the Balance Sheet and provided a BANK statement showing that the balance of this account, as of December 30, 2005, was $$$$$.[11] Including this asset on the Balance Sheet would increase the taxpayer's "total assets" amount, as of December 31, 2005, to $$$$$, which would result in a revised "net worth" of negative $$$$$.

16. Fourth, the Division contends that TAXPAYER-1 undervalued another of his assets on the Balance Sheet. TAXPAYER-1 listed the value of his personal residence to be $$$$$, which is close to the $$$$$ value at which the property was assessed by the Utah County Assessor's Office ("Assessor's Office")

9 Exhibit R-4.

10 IRC §108(b) provides that the amount of debt cancellation income excluded from taxation shall be applied to reduce certain tax attributes of the taxpayer.

for the 2005 tax year.[12] The Division contends that the value TAXPAYER-1 listed for this asset is too low because it is less than the $$$$$ of mortgages he owed on the property, as listed on the liabilities side of the Balance Sheet. The taxpayer claims that the home was "underwater" because he owed more on it than it was worth. The Commission is aware that prior to the economic crisis of the later 2000's, a number of properties were considered to be "underwater." In addition, there is no evidence to show whether the mortgages were taken out near the December 31, 2005 date of the Balance Sheet to determine how reflective of fair market value the mortgage amounts were as of that date. It is possible that the mortgages were taken out years before 2005. Without more evidence, the Division's argument that the Balance Sheet should be revised to reflect an asset value for the personal residence that is equal to the $$$$$ of mortgage liability is not convincing.

17. That being said, it may be appropriate to increase the asset value of TAXPAYER-1's personal residence on the Balance Sheet from $$$$$ to $$$$$. The $$$$$ value at which the Assessor's Office assessed the property for 2005 is an estimate of its value as of January 1, 2005.[13] Taxpayer's Exhibit P-1, however, also shows that the County Assessor's Office assessed the property's 2006 value at $$$$$, which is an estimate of its value on January 1, 2006. The December 31, 2005 date of the Balance Sheet is only one day prior to the January 1, 2006 date on which the County estimated the subject's 2006 value to be $$$$$. As a result, this $$$$$ value is a better reflection of this property's value as of the December 31, 2005 date of the Balance Sheet than the $$$$$ value the taxpayer listed as an asset.[14] If the Balance Sheet is further revised (i.e., after the first revision reflected in Finding of Fact #15) to reflect a $$$$$ value for this asset, the

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11 Exhibit P-1.

12 Exhibit P-1.

13 Utah Code Ann. §59-2-103(1) provides that property is assessed and taxed on its fair market value, as valued on January 1. As a result, the subject's 2005 assessed value of $$$$$ reflects its value on January 1, 2005.

14 Clearly, the property's 2006 assessed value would have been known to the taxpayer in 2009 when he filed his 2005 federal return. Exhibit R-3.

taxpayer's total assets would amount to $$$$$ and his total liabilities would amount to $$$$$, resulting in a net worth of negative $$$$$.[15]

18. Fifth, the Division also questions the values that TAXPAYER-1 listed on the Balance Sheet for the motor vehicles he owned as of December 31, 2005. TAXPAYER-1 listed as assets a VEHICLE-1 worth $$$$$, VEHICLE-2 worth $$$$$, a 1999 VEHICLE-3 worth $$$$$, a VEHICLE-4 worth $$$$$, and three (X) worth $$$$$. TAXPAYER-1 testified that he obtained these values from Blue Book and NADA guides at the time he completed the Balance Sheet. The Division stated that because TAXPAYER-1 has not provided these guides to support the values he listed for these assets, he has not shown that the Balance Sheet is correct and, thus, has not shown that he qualifies to exclude any debt cancellation income from his gross income. The values listed for these older vehicles do not appear unreasonable, and there is no evidence to refute TAXPAYER-1's testimony that he obtained these values from Blue Book and NADA guides. For these reasons, this argument of the Division is not convincing.

19. Sixth, the Division also questions the $$$$$ value that TAXPAYER-1 listed for "furniture, furnishings, clothing, and household items" on the asset side of the Balance Sheet. The Division states that $$$$$ value seems to be a low value for his and his wife's clothing and for the furniture, furnishings, and household items that would have been in his #####-square-foot personal residence. TAXPAYER-1 stated, however, that he went around the home and estimated the price at which he could sell each of these items and arrived at the $$$$$ estimate. There is no evidence to show that this estimate is incorrect. As a result, this argument of the Division is also unconvincing.

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15 The two revisions made to the taxpayer's Balance Sheet results in a revised net worth of negative $$$$$, which is less than the $$$$$ of debt cancellation income that TAXPAYER-1 excluded from taxation. IRC §108(a)(3) provides that the amount of debt cancellation income excluded from taxation "shall not exceed the amount by which the taxpayer is insolvent." So, even if other reasons did not exist to disallow the entire amount of the exclusion the taxpayer claimed (some of which have already been discussed and some of which will be discussed later), this provision would appear to limit the exclusion to $$$$$.

20. Seventh, the Division contends that the Balance Sheet may not be a complete list of all of the taxpayer's assets as of December 31, 2005. The Division contends that had TAXPAYER-1 listed all of his assets, it could have changed his net worth from negative to positive and, thus, disqualified him from claiming any exclusion from taxation in regards to the debt cancellation income. Based on TAXPAYER-1's testimony at the Formal Hearing, this argument is convincing for reasons explained below.

21. TAXPAYER-1 testified that he sold his dental business in 2004 and that he has since worked for dental businesses as an independent contractor. He testified that he has not had an ownership interest in the dental businesses at which he has worked since 2004. However, he testified that he would bring his own "hand pieces" to perform his dental work at these dental businesses. TAXPAYER-1 did not list any dental tools on the Balance Sheet and did not show what the value of these tools would have been as of December 31, 2005. As a result, the taxpayer has not shown that these tools were properly omitted as an asset on the Balance Sheet.

22. Although TAXPAYER-1 did not own an interest in the dental practices at which he worked after 2004, he stated that in 2005, he was the sole owner of DENTAL PRACTICE, an S-corporation. He stated that the PLLC had an account because the dental practices at which he worked would pay his PLLC for his services. The PLLC account was different from TAXPAYER-1's personal account which was discussed earlier and which had a balance of $$$$$. TAXPAYER-1 did not argue that he was not required to list the PLLC's assets on his Balance Sheet. However, he argued that the PLLC owned nothing of value as of the December 31, 2005 date of the Balance Sheet. Although TAXPAYER-1 testified that the PLLC account had no money in it, he did not provide an account statement or other evidence to support his claim. Without such evidence, it is not clear that the taxpayer was insolvent as of the December 31, 2005 date of the Balance Sheet.

23. In addition, TAXPAYER-1 testified that he had a checking account at CREDIT UNION that was attached to a credit card he also had there and that his wife may have had an account at BANK-1. He

stated that his wife had a separate account because she had her own BUSINESS-1.[16] The taxpayer did not provide an account statement to show that neither of these accounts had a zero balance as of December 31, 2005. Without such evidence, it is not clear that the taxpayer was insolvent as of the December 31, 2005 date of the Balance Sheet.

24. The Division also questioned why TAXPAYER-1 would not have listed any other assets on the Balance Sheet, including any proceeds he would have received from the sale of his dental business in 2004. The Division's concern is not unwarranted, especially when it is considered that a Tax Commission Investigator determined that TAXPAYER-1 had substantial income for the 2000 through 2004 tax years that were at issue in his criminal trial.[17]

25. Furthermore, evidence exists to show that TAXPAYER-1 invested $$$$$ with COMPANY-2 in March 2004, specifically a March 1, 2006 letter from NAME-1 informing TAXPAYER-1 that the business transaction in which he invested this money was fraudulent.[18] At the hearing, TAXPAYER-1 testified that he was not aware that the transaction was fraudulent until he received this March 1, 2006 letter from NAME-1. Later, TAXPAYER-1 was asked why he did not list this investment on the December 31, 2005 Balance Sheet if he was not aware that the investment was fraudulent until March 2006. He answered by stating that the March 2006 letter was the first time he had such notice in writing, but that he first became aware that the transaction was fraudulent in a conversation prior to December 31, 2005. TAXPAYER-1's testimony is contradictory, and he provided no document or other evidence to support his subsequent claim that he knew about the fraudulent transaction in 2005. As a result, his first statement that he was not aware of the fraudulent

16 The taxpayer's 2005 federal return shows the business name of his wife's BUSINESS-1 as NAME OF BUSINESS-1. Exhibit R-3. TAXPAYER-1 testified that his wife's BUSINESS-1 was also a sole proprietorship.

17 Exhibit R-20, p. 51 (the investigation revealed that TAXPAYER-1 had annual income ranging between $$$$$ and $$$$$ for these five years).

18 Exhibit P-7. This investment of $$$$$ is at the center of another issue in this appeal (i.e., Issue 7) and, as a result, will be discussed in more detail later in the decision.

transaction until March 2006 is more persuasive. For these reasons, TAXPAYER-1 has not shown that the $$$$$ investment was properly excluded from the December 31, 2005 Balance Sheet he compiled. Adding this $$$$$ asset would change the taxpayer's net worth from negative to positive and would disqualify him from claiming an exclusion from taxation for the $$$$$ of debt cancellation income.

26. At the hearing, TAXPAYER-1 testified that "about 2005," he bought a second residence that was financed by the seller (which is a cabin that will be addressed in more detail later in Issue 5). Based on this testimony, it is possible that he purchased the cabin after 2005 because he also stated that he did not know when he purchased it. However, TAXPAYER-1's testimony also indicates that he may have owned this cabin in 2005. If so, he omitted it from both the assets and the liabilities portions of the December 31, 2005 Balance Sheet. As a result, TAXPAYER-1's testimony about the cabin also suggests that the Balance Sheet may be incomplete and discounts his assertion that he was insolvent in 2005 when the debt at issue was cancelled.

27. Based on the foregoing, TAXPAYER-1 has not shown that the December 31, 2005 Balance Sheet on which he showed his net worth to be negative $$$$$ is correct. Nor has he shown that it reflects his net worth "immediately before the discharge" of the cancelled debt because no evidence was submitted to show when the debt was cancelled. In addition, TAXPAYER-1 has not shown that he properly reduced his tax attributes by the applicable amount associated with the exclusion from taxation of the debt cancellation income. Finally, for numerous reasons discussed earlier, TAXPAYER-1 has not shown that he included all of his or his wife's assets on the Balance Sheet. For these reasons, TAXPAYER-1 has not met his burden of proof to show that the Division's action to disallow his exclusion of the $$$$$ of debt cancellation income from taxation is incorrect. This assessment of this item on the Division's 2005 assessment should be sustained.

Issue 2: Depreciation for VEHICLE-5 - 2007 Tax Year

28. For the 2007 tax year, the Division disallowed a depreciation expense of $$$$$ that

TAXPAYER-1 had claimed for a VEHICLE-5 he purchased that year.[19] This is one of two items on the Division's 2007 assessment that the taxpayer is contesting (the second contested item for 2007 will be addressed in Issue 3).

29. In addition to TAXPAYER-1's profession as a dentist, he has a real estate business for which he reported gains, losses, and expenses on his tax returns. For the 2007 tax year, the taxpayer claimed a depreciation expense of $$$$$ on Schedule C of his federal return for this business.[20] TAXPAYER-1 claims that he was entitled to take the depreciation expense for a VEHICLE-5 he purchased in 2007 and used in his real estate business. He also claims that IRC §179 allows a small business to deduct all of the depreciation for a vehicle used in that business in the first year that the vehicle is owned.

30. TAXPAYER-1 submitted evidence to show that he purchased a 2008 VEHICLE-5 on December 10, 2007 for $$$$$. The taxpayer determined that under IRC §179, he could depreciate 77.68% of the purchase price because this is the percentage of miles that the truck was driven for a business purpose in comparison to the total miles it was driven in its first year (i.e., in 2007). The taxpayer states that the VEHICLE was driven a total of ##### total miles in 2007 and that ##### of these miles were for a business purpose, which equates to 77.68% of the total miles.[21] The taxpayer claims that the allowable depreciation amount can be determined by multiplying the 77.68% ratio by the $$$$$ purchase price of the truck. This calculation results in a depreciation expense of $$$$$, which is higher than the $$$$$ amount the taxpayer claimed on his return.[22] The taxpayer did not explain how he determined the $$$$$ depreciation amount he reported on his 2007 federal return.

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19 Exhibit R-8.

20 Exhibit R-10.

21 To support these mileages, the taxpayer submitted a 2007 VEHICLE Worksheet for Schedule C – Real Estate Development. Exhibit P-2.

22 On Exhibit P-2, the taxpayer showed that this calculation would result in a depreciation amount of $$$$$. It appears, however, that the taxpayer mistakenly multiplied the VEHICLE-5 purchase price by a 76.68% ratio to derive this amount of depreciation.

31. The Division admits that the IRS accepted the taxpayer's 2007 federal return and has not audited TAXPAYER-1's claim that he qualified for the depreciation expense at issue. In addition, the Division admits that IRC §179 would allow the taxpayer to deduct the $$$$$ depreciation expense he claimed if he were to provide sufficient evidence to support the mileage amounts with which he calculated the 77.68% ratio he applied to the VEHICLE-5 purchase price. The Division, however, contends that the taxpayer's evidence is insufficient to support these mileage amounts and to show that in 2007, the VEHICLE-5 was driven for ##### total miles and that ##### of these miles were for a business purpose. As a result, this issue does not involve an interpretation of law. It involves the evidence the taxpayer submitted and a determination of whether that evidence is sufficient to show that these are the correct mileages with which to calculate the depreciation expense.

32. The taxpayer does not provide any documentary evidence to support his claim that the VEHICLE-5 was driven for a total of ##### miles in 2007. Because the VEHICLE-5 was purchased on December 10, 2007, it is plausible that the VEHICLE-5 might not have been driven more than ##### miles in 2007. However, the taxpayer did not indicate when he took a final odometer reading to obtain this total mileage. The taxpayer stated that he wrote his 2007 mileage down on a calendar so that it was available to him in 2009 when he filed his 2007 returns.[23] However, he did not provide this calendar as evidence at the Formal Hearing.

33. The taxpayer also proffers little documentary evidence to support his claim that the VEHICLE-5 was driven ##### miles in 2007 for real estate business purposes. The taxpayer testified that he drove the VEHICLE-5 from his home in CITY-1, Utah to CITY-2, Utah for a business purpose, specifically to look at condominiums being built in CITY-2 by a company named COMPANY-1 ("COMPANY-1"). He stated that he went to CITY-2 to look at the condominiums being built because he had purchased two condominiums from

23 The IRS transcript for the taxpayer's 2007 account shows that he filed his 2007 federal return on June

COMPANY-1 in February 2007 that were to be built in CITY-3, Utah and because the ones in CITY-2 were being built first. He stated that a friend of his in his ward, NAME-2, owned the company from which he had purchased the two CITY-3 condominiums and that NAME-2 told him that he could look at the condominiums he was building in another of his developments in CITY-2. TAXPAYER-1 stated that he went to CITY-2 by himself and that he was able to walk through COMPANY-1's construction site in CITY-2 without anyone's assistance. TAXPAYER-1 did not know if the condominiums being built in CITY-2 were available for sale when he went there and did not indicate that he was contemplating an investment in the CITY-2 properties.

34. To support this claim that he drove the VEHICLE-5 ##### miles for business purposes, TAXPAYER-1 provided a Google map showing that the distance between CITY-1 and CITY-2 is #####-miles one-way (#####-miles round-trip).[24] Again, however, TAXPAYER-1 did not provide the calendar on which he recorded this mileage to support his claim. He also did not provide any gas receipts for the trip. Nor did he provide any documentary evidence to support his testimony that COMPANY-1 built condominiums in CITY-2 or that NAME-2 told him he could drive to CITY-2 to see the construction taking place out there. Had TAXPAYER-1 provided some documentary evidence to support the mileages or his testimony about the business purpose, perhaps his position would be stronger. Without such evidence, however, the Commission is not sufficiently convinced of the mileages the taxpayer used to calculate his depreciation expense for the VEHICLE-5.

35. Based on the foregoing, the Commission finds that the taxpayer has not shown that he drove the VEHICLE-5 for ##### total miles in 2007 or that ##### of these miles were for a business purpose. Accordingly, the Commission finds that the taxpayer has not shown that the $$$$$ depreciation expense he claimed for the VEHICLE-5 in 2007 was appropriate.

15, 2009. Exhibit R-10.

Issue 3: Sale of a Cabin – 2007 Tax Year

36. For the 2007 tax year, the Division disallowed a portion of the "costs of goods sold" deduction that TAXPAYER-1 claimed when calculating his gross income for the sale of a cabin. Specifically, the Division disallowed $$$$$ of the cost of goods sold amount of $$$$$ that the taxpayer had claimed.[25] This is the second of two items on the Division's 2007 assessment that the taxpayer is contesting (the other item being the one addressed in Issue 2). The Division admits that the IRS accepted the taxpayer's 2007 federal return and has not audited the cost of goods sold amount that TAXPAYER-1 claimed for the sale of the cabin.

37. TAXPAYER-1 testified that he purchased a cabin in CITY-4 in Utah in May 2007 for $$$$$. He testified that while he bought the cabin in his name, he bought it for him and his son, NAME-4, to remodel and to sell. He stated that they gutted the inside of the cabin, which also included putting in new flooring and floor joists and adding a second bathroom. He also stated that they excavated the lot, worked on the cabin's water supply, and installed new siding on the cabin's exterior. TAXPAYER-1 stated that his son NAME-4 incurred many of the expenses while they were remodeling the cabin and that NAME-4 expended more time on the remodel than he did. TAXPAYER-1 testified that he sold the cabin on September 20, 2007 for $$$$$.

38. TAXPAYER-1 submitted a Schedule C from his 2007 federal return on which he reported the cabin's sales price to be $$$$$, the cost of goods sold amount to be $$$$$, and his gross profit on the sale to be $$$$$. He also provided a Schedule C supporting statement for the $$$$$ cost of goods sold, on which he showed how this amount was determined, as follows:[26]

Cost		$$$$$
Broker Fees		$$$$$
Remodel Cost		$$$$$
NAME-4		$$$$$
	Total	$$$$$

24 Exhibit P-2.
25 Exhibit R-8.
26 Exhibit P-3.

39. The Division could not explain exactly how it determined that $$$$$ of the $$$$$ amount should be disallowed. However, it asked the Commission to sustain this portion of its assessment because TAXPAYER-1 did not provide documents to show the price at which he sold the cabin or documents to support the various amounts that comprised his cost of goods sold amount.

40. TAXPAYER-1 did not provide the contracts and checks that the Division asked for. However, TAXPAYER-1 submitted a copy of a check he wrote to NAME-4 in the amount of $$$$$ to show that he paid NAME-4 to compensate him for his portion of the profits and for the supplies and construction materials that NAME-4 had purchased. The check is dated October 1, 2007, which is about 10 days subsequent to the September 20, 2007 date on which the cabin was sold. TAXPAYER-1 also provided a statement signed by NAME-4 in which NAME-4 attested that the $$$$$ check was for the remodel and subsequent sale of the cabin at issue.[27]

41. To further show that NAME-4 was a partner with him in the cabin, TAXPAYER-1 submitted portions of NAME-4's 2007 federal return, on which NAME-4 and his wife reported a Schedule D capital gain from the sale of a cabin. They reported the sales price of the cabin to be $$$$$, the "cost or other basis" to be $$$$$, and their gain to be $$$$$.[28] It appears that NAME-4 was only reporting amounts to represent his "half" of their enterprise to remodel and sell the cabin. The $$$$$ sales price he reported is about one-half of the $$$$$ sales price that TAXPAYER-1 reported and supports the sales price reported by TAXPAYER-1.

42. In addition, TAXPAYER-1 provided a breakout of the "cost or other basis" amount of $$$$$ that NAME-4 reported on Schedule D of his federal return, as follows:[29]

Cost	$$$$$
Broker Fees	$$$$$

27 Exhibit P-3.
28 Exhibit P-3.
29 Exhibit P-3.

Remodel Cost	$$$$$
Total	$$$$$

43. With one exception, the amounts that NAME-4 reported on his federal return support the amounts that comprised the costs of goods sold amount that TAXPAYER-1 reported on his return. First, the $$$$$ amount that NAME-4 reported as the cost of the cabin is exactly 50% of the $$$$$ cost that TAXPAYER-1 reported. This information is sufficient to support this one component of TAXPAYER-1's cost of goods sold.

44. Second, the $$$$$ amount that NAME-4 reported as broker fees is exactly 50% of the $$$$$ of broker fees that TAXPAYER-1 reported. This information is also sufficient to support this component of TAXPAYER-1's cost of goods sold.

45. Third, NAME-4 reported a gain of $$$$$ on his federal return, which is close to the $$$$$ amount TAXPAYER-1 reported as one of the components of his cost of goods sold and which he described as "NAME-4." When this is considered in concert with the check TAXPAYER-1 wrote to NAME-4 and the information NAME-4 has provided, the information is sufficient to also support the $$$$$ amount that TAXPAYER-1 claimed as another component of his cost of goods sold.

46. The last component of TAXPAYER-1's cost of goods sold is the remodel cost that he reported to be $$$$$. TAXPAYER-1 has not provided any receipts to the Commission to support this amount of remodel costs. However, NAME-4 reported the remodel cost to be $$$$$. Because NAME-4 was reporting cost amounts that were 50% of the amounts that TAXPAYER-1 was reporting, the information is sufficient to support $$$$$ of the remodel costs (two times the $$$$$ of remodel costs reported by NAME-4) that TAXPAYER-1 reported. However, it is insufficient to support the $$$$$ of additional remodel costs that TAXPAYER-1 reported on his return ($$$$$ minus $$$$$).

47. For this issue, TAXPAYER-1 provided some documentary evidence to support his testimony. In addition, the Division could not explain how it determined its assessment amount of $$$$$. Based on the foregoing, TAXPAYER-1's evidence is sufficient, by a preponderance of the evidence, to support all but $$$$$ of the cost of goods sold amount that he reported to the IRS. As a result, his evidence is sufficient to show that the Division's disallowance of $$$$ $of the cost of goods sold amount he reported should be reduced. The Division's assessment should be revised to reflect a cost of goods sold disallowance of only $$$$$.

Issue 4: Sale of a Recreational Lot – 2009 Tax Year

48. For the 2009 tax year, the Division disallowed a portion of the cost of goods sold amount that TAXPAYER-1 claimed when reporting his gross income for the sale of a recreational lot. Specifically, the Division disallowed $$$$$ of the cost of goods sold amount of $$$$$ that the taxpayer claimed.[30] This is the first of three items on the Division's 2009 assessment that the taxpayer is contesting (the other two items will be addressed as Issues 5 and 8). The Division admits that the IRS accepted the taxpayer's 2009 federal return and has not audited the cost of goods sold amount that TAXPAYER-1 claimed for the sale of the recreational lot.

49. TAXPAYER-1 stated that he sold a recreational lot he owned in CITY-4 on July 7, 2009. On Schedule C of his 2009 federal return, TAXPAYER-1 reported that he earned $$$$$ of gross profit on the sale based on a sales price of $$$$$ and a cost of goods sold of $$$$$.[31] As a result, the Division allowed $$$$$ of the $$$$$ cost of goods sold amount that TAXPAYER-1 reported, but disallowed the remaining $$$$$.

50. TAXPAYER-1 testified that he purchased the lot in 2004 for the $$$$$ amount he reported as the lot's cost of goods sold. He also testified that he purchased the lot from NAME-5. TAXPAYER-1 did not

30 Exhibit R-11.

31 Exhibit R-13.

provide a settlement statement or other document to show the price at which he purchased the lot from NAME-5. In addition, he stated that he does not recall how he paid NAME-5 for the lot and that he has not attempted to see if his bank would have copies of checks to support payments totaling $$$$$. However, to substantiate the purported purchase price of $$$$$, TAXPAYER-1 obtained a signed letter from NAME-5 dated November 13, 2013 on which NAME-5 listed her address and telephone number.[32] In the letter, NAME-5 stated the following:

> I sold to TAXPAYER-1 my lot ##### at CITY-4 Association on or about June 2004 for the price of $$$$$. Since it has been over 9 years ago I don't have any remaining tax records but can assure you I sold the lot for $$$$$.

51. The Division asks the Commission not to accept TAXPAYER-1's claim that he purchased the lot for $$$$$. First, the Division contends that the Commission should not find that NAME-5 letter shows that she sold the lot to TAXPAYER-1 for $$$$$ because she has not affirmed that her statements are true either by having her statements notarized or by affirming or attesting to the truth of her statements. Second, the Division states that it has only seen three checks that TAXPAYER-1 paid to NAME-5, two in the amounts of $$$$$ each and one in the amount of $$$$$. Because the checks it has seen only amount to $$$$$, the Division contends that TAXPAYER-1's evidence is insufficient to show that he paid $$$$$ for the lot.

52. Without a settlement statement or checks written to NAME-5 totaling $$$$$, there is still some doubt as to the price TAXPAYER-1 paid in 2004 for the lot. However, TAXPAYER-1 has provided some documentary evidence to support his testimony and the $$$$$ cost of goods sold amount that he reported to the IRS, specifically the letter from NAME-5. The Division questioned the evidentiary value of the letter, but has provided no information to show that the letter should be given little or no weight because it was not notarized and does not contain words indicating that the author is attesting or affirming her statements to be true. Nor does the Division appear to have tried to contact NAME-5 to inquire about the accuracy of her letter,

32 Exhibit P-4.

even though she provided her telephone number and address on the letter. For these reasons and based on a preponderance of the evidence standard, TAXPAYER-1 has met his burden to show that he paid $$$$$ for the lot at issue, which supports the $$$$$ cost of goods sold amount he reported to the IRS. Accordingly, the Commission should reverse that portion of the Division's 2009 assessment concerning the recreational lot that TAXPAYER-1 sold in 2009.

Issue 5: Mortgage Interest Deduction – 2009, 2010 and 2011 Tax Years

53. For the 2009, 2010, and 2011 tax years, the Division disallowed all or a portion of the mortgage interest that the taxpayer claimed as itemized deductions concerning a second residence that he owned. Specifically, the Division disallowed interest deductions in the amount of $$$$ for 2009, $$$$$ for 2010, and $$$$$ for 2011.[33] This is the second of three items on the Division's 2009 assessment that the taxpayer is contesting (the other two items being Issue 4, which was previously addressed, and Issue 8, which will be addressed later). This is the only item on the Division's 2010 assessment that the taxpayer is contesting. This is the first of two items on the Division's 2011 assessment that the taxpayer is contesting (the other item will be addressed later as Issue 9).

54. The Division admits that the IRS accepted the taxpayer's 2009 and 2011 federal returns and has not audited the interest deductions that TAXPAYER-1 claimed for these years. The Division also stated that the IRS has audited the taxpayer's 2010 federal return, but indicated that it does not know if the IRS changed the interest deduction that TAXPAYER-1 took for this year. The Division did not submit an IRS account statement for 2010 to show that the IRS audit for this year involved the interest deduction at issue.

55. TAXPAYER-1 stated that "about 2005," he purchased a cabin at CITY-4 as a second residence (which is a different cabin than the one that he remodeled and sold in 2007, which was discussed in Issue 3). TAXPAYER-1 stated that he purchased this cabin from NAME-6, who financed the purchase. On

33 Exhibits R-11, R-14, and R-17.

his 2009, 2010, and 2011 federal tax returns, TAXPAYER-1 deducted interest he paid on the cabin as itemized deductions in the amounts of $$$$$ for 2009, $$$$$ for 2010, and $$$$$ for 2011.[34]

56. To show that he made interest payments on the cabin during 2009, 2010, and 2011, TAXPAYER-1 submitted a letter dated September 5, 2014 that his accountant, REPRESENTATIVE FOR TAXPAYER's, wrote to NAME-6. In the letter, REPRESENTATIVE FOR TAXPAYER's informs NAME-6 that one of the issues in TAXPAYER-1's audit with the Tax Commission is the cabin purchase between the taxpayer and NAME-6. REPRESENTATIVE FOR TAXPAYER's ask NAME-6 to "provide an affidavit" stating that he received interest payments from TAXPAYER-1 totaling $$$$$ for 2009, $$$$$ for 2010, and $$$$$for 2011.[35]

57. TAXPAYER-1 also submitted NAME-6's response to REPRESENTATIVE FOR TAXPAYER's request.[36] NAME-6 did not provide the "affidavit" REPRESENTATIVE FOR TAXPAYER's requested. Instead, NAME-6 provided a copy of Schedule B from his and his wife's federal return for each of the 2009, 2010, and 2011 tax years. These schedules show that NAME-6 reported interest income from taxpayer-1 in the amount of $$$$$ for 2009, $$$$$ for 2010, and $$$$$ for 2011. NAME-6 also wrote a short statement in which he indicated, "After reviewing with my accountant these are figures we actually used on my return."

58. The Division points out that under IRC 163(a), only interest that is paid is allowable as a deduction. The Division questions whether the amounts that NAME-6 reported on his returns as interest were instead rental income because the payments were made after the purchase agreement between TAXPAYER-1

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34 Exhibits R-13, R-16, and R-19.
35 Exhibit P-5. The amounts TAXPAYER-1 asked NAME-6 to verify for 2009 and 2011 are less than the amounts TAXPAYER-1 claimed as itemized deductions on his returns for these years.
36 Exhibit P-5.

and NAME-6 expired.[37] The Division has not provided any information to show that the IRS would consider the payments to be rental income instead of interest. In addition, TAXPAYER-1 argued that had the payments been rental income, NAME-6 would have reported the payments as rental income on another portion of his federal returns and not on Schedule B. This argument is persuasive and supports the taxpayer's assertion that he and NAME-6 agreed for him to continue making interest payments after the May 1, 2009 expiration date of the cabin purchase agreement.

59. The Division also objects to the statement NAME-6 wrote to verify the interest amounts about which he was asked because NAME-6 did not swear that his statement was true and because he provided no address. Regardless of these objections, the amounts NAME-6 was verifying are supported by the Schedule B's that he provided from his own federal returns for 2009, 2010, and 2011.

60. In addition, the Division argued that none of these interest payments should be allowed unless TAXPAYER-1 provides checks showing that he paid these amounts. The Division stated that it had access to some of TAXPAYER-1's cancelled checks from 2009 that totaled $$$$$. As a result, it allowed $$$$$ of the $$$$$ interest deduction TAXPAYER-1 claimed for the cabin on his 2009 federal return (thus disallowing the remaining $$$$$). The Division stated that it did not allow any interest payments on the cabin for 2010 and 2011 because it did not have access to any cancelled checks from these years. The Division asks the Commission not to allow any more of the interest deductions that TAXPAYER-1 claimed for the cabin in 2009, 2010, and 2011 without checks to verify that he actually made the payments. This argument of the Division, however, is also not persuasive. It is unlikely that NAME-6 would have reported interest income had he not received the payments from TAXPAYER-1. As a result, the Commission finds that, by a

37 In the letter to NAME-6, REPRESENTATIVE FOR TAXPAYER's indicates that the cabin purchase agreement expired on May 1, 2009. He also indicates in the letter that TAXPAYER-1 contends that the parties agreed to continue the contract by allowing TAXPAYER-1 to continue making the interest payments after May 1, 2009.

preponderance of the evidence, TAXPAYER-1 paid interest on the cabin in the amounts of $$$$$ for 2010, $$$$$ for 2011, and $$$$$ for 2011.

61. For 2009, TAXPAYER-1's evidence is sufficient to show that he paid $$$$$ of interest to NAME-6 for the cabin that year. However, it is insufficient to show that he paid the entire $$$$$ of interest he claimed as an itemized interest deduction that year. There is no evidence to show that the $$$$$ of cancelled checks the Division was aware of were in addition to and not part of the $$$$$ of interest income reported by NAME-6. As a result, the Commission finds that the portion of the Division's 2009 assessment disallowing $$$$$ of the interest deduction amount of $$$$$ should be revised. The assessment should be revised to reflect a disallowance of only $$$$$ (the $$$$$ that TAXPAYER-1 claimed minus $$$$$).

62. For 2010, TAXPAYER-1's evidence is sufficient to show that he paid $$$$$ of interest to NAME-6 for the cabin that year. As a result, TAXPAYER-1 has shown that he made all of the interest payments that he claimed on his 2010 federal return. As a result, the Commission finds that the portion of the Division's 2010 assessment disallowing the $$$$$ interest deduction TAXPAYER-1 claimed for the cabin should be reversed.

63. For 2011, TAXPAYER-1's evidence is sufficient to show that he paid $$$$$ of interest to NAME-6 for the cabin that year. However, it is insufficient to show that he paid the entire $$$$$ of interest he claimed as an itemized interest deduction that year. As a result, the Commission finds that the portion of the Division's 2011 assessment disallowing the entire interest deduction TAXPAYER-1 claimed for the cabin should be revised. The assessment should be revised to reflect a disallowance of only $$$$$ (the $$$$$ that TAXPAYER-1 claimed minus $$$$$).

Issue 6: Mileage Deduction for Work Travel - 2008, 2009, 2010 and 2011 Tax Years

64. At the Initial Hearing, the taxpayer claimed that he was entitled to a mileage deduction for work travel that he had failed to claim on his federal returns and that the Division had not addressed in its

assessments for the 2008, 2009, 2010, and 2011 tax years. At the Formal Hearing, the taxpayer stated that he was no longer asking the Commission to find that he was entitled to this deduction for any of these years. As a result, this issue will not be addressed in the Formal Hearing decision. Because this issue was addressed as "Issue 6" in the Initial Hearing Order, it may be confusing to label one of the Formal Hearing issues as "Issue 6." Accordingly, none of the issues contested at the Formal Hearing will be labeled as "Issue 6."

65. The mileage deduction issue was the only issue at the Initial Hearing that the taxpayer contested in regards to the Division's 2008 assessment. Because the taxpayer is no longer contesting this issue at the Formal Hearing, the taxpayer is no longer contesting any portion of the Division's 2008 assessment. Accordingly, the Commission should sustain the Division's 2008 assessment in its entirety.

Issue 7: Investment Fraud Loss – 2006 Tax Year

66. For the 2006 tax year, the Division disallowed an investment fraud loss in the amount of $$$$$ that the taxpayer had claimed as an adjustment to his federal adjusted gross income.[38] This is the only item on the Division's 2006 assessment that the taxpayer is contesting. The Division asserts that the taxpayer has not shown that he qualifies for the investment fraud loss adjustment under IRC §165.

67. On line 14 of his 2006 federal return, the taxpayer claimed a loss of $$$$$ and indicated that he was attaching a Form 4684. The Form 4684 that the taxpayer attached to his return shows that he was claiming a casualty or theft loss of $$$$$ resulting from investment fraud.[39] TAXPAYER-1 stated that a friend of his named NAME-1 encouraged him to invest in a company named COMPANY-2, after which TAXPAYER-1 "gave" NAME-1 $$$$$ in 2004 to invest into the company. TAXPAYER-1 did not submit information showing whether it was himself, NAME-1, or some other entity who made the actual investment of the $$$$$ in COMPANY-2.

68. TAXPAYER-1, however, did submit a letter he received from COMPANY-3 ("COMPANY-

38 Exhibit R-5.

3") that was signed by NAME-1 and dated March 1, 2006 ("2006 Letter").[40] In this letter, NAME-1 informed TAXPAYER-1 of the following (in pertinent part):

> I regret to inform you that the business transaction, where you invested $$$$$ in March 2004, in which we entered into an agreement with COMPANY-2 is no longer feasible because the entire transaction was fraudulent.
>
> The funds were invested with COMPANY-2 to pay bank fees for a Standby Letter of Credit (SLC) that would be used as collateral with the manufacturer, MANUFACTURER. .
>
> The SLC was found to be fraudulent and the Company that issued the Purchase Order did not exist. . . .
>
> Each time I presented an SLC, it was a fake. Finally, by having COMPANY-2 send the SLC directly to the bank, the banker was able to verify that it was fake, turned the paper over to Interpol and advised me to take my case to the FBI of their fraudulent activities.
>
> I provided many documents, emails, and copies of fraudulent collateral to the FBI office in CITY-5. . . .

69. TAXPAYER-1 contends that the 2006 Letter not only shows that he invested $$$$$, but also that his investment turned out to be fraudulent. This letter is sufficient to support TAXPAYER-1's claim that he made some sort of arrangement with COMPANY-3 to invest $$$$$ in 2004. This letter, however, does not show whether he invested in COMPANY-2 directly or whether he invested the money in COMPANY-3 which subsequently invested it in COMPANY-2. Because few, if any, details of the business arrangement between TAXPAYER-1 and COMPANY-3 are known, it is unclear whether TAXPAYER-1, COMPANY-3, or some other entity owned the $$$$$ that was purportedly stolen by COMPANY-2. The 2006 Letter, however, is sufficient to show that by March 2006, a problem had arisen with the $$$$$ that TAXPAYER-1 or some entity with whom he was associated had invested in COMPANY-2.

70. To further support his claim that his $$$$$ investment was fraudulently lost, TAXPAYER-1 submitted another letter from NAME-1 dated September 29, 2014 ("2014 Letter").[41] In this letter, NAME-1 informed TAXPAYER-1 of the following (in pertinent part):

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39 Exhibit R-7.
40 Exhibit P-7.
41 Exhibit P-7.

> I have been in contact with the CITY-6 office and the Salt Lake City office of the FBI to try and obtain a statement from them to verify the fact that I filed a fraud complaint.
>
> I filed the fraud complaint, December 1, 2004 with [an agent] in the CITY-5, State-1 office against NAME-7 of COMPANY-4 of CITY-7, STATE-2.
>
> Since the CITY-5 office is now closed, I have contracted NAME-8 in CITY-6, who can verify this. . . .

TAXPAYER-1 also submitted emails from NAME-1 to the FBI asking for a copy of the fraud complaint that NAME-1 filed in 2004.[42]

71. The 2014 Letter and the emails to the FBI suggest that NAME-1 filed a fraud complaint with the FBI in 2004. However, these documents also indicate that the complaint was filed against Name-7 and COMPANY-4 of CITY-7, STATE-2 ("NAME-7"), an entity that was not mentioned in the 2006 Letter from NAME-1. The 2006 Letter indicated that TAXPAYER-1 had invested $$$$$ in COMPANY-2 in 2004. It is unknown whether the NAME-7 entity against whom NAME-1 filed a complaint is related in any way to the COMPANY-2 entity in which TAXPAYER-1 appears to have invested his $$$$$. Nevertheless, if the complaint NAME-1 filed with the FBI in 2004 against the NAME-7 entity was related to the COMPANY-2 investment, it seems odd that NAME-1 waited more than a year to send the 2006 Letter in which he informed TAXPAYER-1 that the business transaction with COMPANY-2 was no longer feasible and that he had provided documents to the FBI. Without more information, it is not clear that the FBI complaint filed in 2004 was related to TAXPAYER-1's investment of $$$$$ with COMPANY-2.

72. The taxpayer also provided no testimony or documentary evidence to show the outcome of the complaint that NAME-1 filed with the FBI in 2004. There is no evidence to show whether the FBI investigated the complaint, much less to show whether fraud or theft charges were eventually filed against any entity in regards to the $$$$$ investment. There is also no evidence to show whether an entity actually violated state or federal fraud or theft law.

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42 Exhibit P-7.

73. TAXPAYER-1's information is also insufficient to show when he discovered the purported fraud or theft associated his $$$$$ investment. If the complaint filed against the NAME-7 entity involved the $$$$$ at issue, it is clear in the 2014 Letter that NAME-1 discovered it in 2004. It is less clear when TAXPAYER-1 discovered the purported fraud or theft because his testimony on the matter was contradictory. Initially, TAXPAYER-1 testified that he did not become aware of the fraud or theft until March 2006, when he received NAME-1's 2006 Letter. Later, he testified that NAME-1 had informed him of the fraud or theft prior to the December 31, 2005 date of the Balance Sheet he prepared (which was discussed earlier for Issue 1). For these reasons, it is not clear that any fraud or theft associated with the $$$$$ was discovered in 2006, the year in which TAXPAYER-1 claimed the $$$$$ loss.

74. The Division contends that even if NAME-1 filed a fraud complaint with the FBI regarding TAXPAYER-1's $$$$$$ investment, TAXPAYER-1's information is insufficient to qualify as an investment fraud theft loss that can be deducted for tax purposes. First, the Division claims that TAXPAYER-1's information is insufficient to satisfy IRS §165(e), which requires a loss arising from theft to be treated as sustained during the taxable year in which the taxpayer discovers such loss. For reasons discussed in the prior paragraph, this argument of the Division is persuasive.

75. Second, the Division contends that the taxpayer's information is insufficient to satisfy requirements to claim a theft loss, as discussed in Rev. Rul. 72-112, 1972-1 C.B. 60 ("Rev. Rul. 72-112"). The Division points out that to qualify as a "theft" loss, the ruling requires the taxpayer "to prove that his loss resulted from a taking of property that is illegal under the law of the state where it occurred and that the taking was done with criminal intent." Because TAXPAYER-1 did not discuss what constitutes "theft" in the jurisdiction in which the purported theft occurred and did not show that the alleged perpetrator's actions met these elements, the Division contends that the taxpayer has not satisfied the requirements to claim a loss from theft. The Division claims that NAME-1's assertion that a fraudulent action occurred should be discounted

because there was no evidence showing what qualifications NAME-1 had, if any, to determine that the actions of another were fraudulent. In addition, the Division contends that TAXPAYER-1 has not shown that the alleged perpetrator took the $$$$$ at issue "with criminal intent."

76. The arguments of the Division, as discussed in the prior paragraph, are also persuasive. TAXPAYER-1 has not shown that the taking of his $$$$$ was illegal under the law and not merely an investment that went bad. The taxpayer has also not shown the elements required for the taking to be considered illegal under the laws of the appropriate jurisdiction, nor has he provided sufficient details about the transaction to determine whether or not the taking was illegal. Furthermore, there is no evidence to show that the FBI even filed charges against an entity or whether any entity was found to have violated a law in regards to the $$$$$ investment. In addition, because there were few, if any, details provided about the transaction, TAXPAYER-1 has also not shown that the taking was done with "criminal intent." It is not known what actions the NAME-7 entity against whom NAME-1 filed a complaint took, much less whether its actions were done with criminal intent. Lastly, NAME-1's assertion that fraud occurred is not persuasive because there is no evidence to suggest that either NAME-1 or the banker mentioned in the 2006 Letter was qualified to make such a determination. For these reasons, TAXPAYER-1 has not shown that he lost his $$$$$ investment because of fraud or theft.

Issue 8: Deductions for Training and Seminars – 2009 Tax Year

77. For the 2009 tax year, the Division disallowed $$$$$ of "other expenses" the taxpayer claimed in regards to his real estate development business.[43] This is the third of three items on the Division's 2009 assessment that the taxpayer is contesting (the other two items being Issues 4 and 5, which were previously addressed). The Division admits that the IRS accepted the taxpayer's 2009 federal return and has not audited

43 Exhibit R-11. On the Statutory Notice, the Division described this portion of the assessment as a disallowed investment fraud loss. Both parties agree that this portion of the 2009 assessment actually relates to the $$$$$ of other expenses that the taxpayer claimed on Schedule C of his 2009 federal return.

the $$$$$ of "other expenses" at issue.

78. TAXPAYER-1 claimed the $$$$$ of "other expenses" on Schedule C of his 2009 federal return, on which he also provided information to show that these expenses were comprised of four items, specifically:[44]

Fees		$$$$$
Seminar		$$$$$
Seminar		$$$$$
Seminar		$$$$$
	Total	$$$$$

79. TAXPAYER-1 did not remember what the fee expense of $$$$$ or the seminar expense of $$$$$ was for. However, he testified that the $$$$$ expense was for a seminar he purchased from BUSINESS-2 (a NAME-9 program) and that the $$$$$ expense was for a seminar he purchased from BUSINESS-3("BUSINESS-3"). The amounts TAXPAYER-1 claims to have paid for the BUSINESS-2 and BUSINESS-3 seminars total $$$$$. As a result, TAXPAYER-1 asks the Commission to allow at least $$$$$ of the $$$$$ of "other expenses" he claimed on Schedule C of his 2009 federal return.

80. TAXPAYER-1 has no recollection of what the $$$$$ fee expense or the $$$$$ seminar expense was for and submitted no testimony or evidence to support his deduction of these expenses on his federal return. In addition, there is no evidence to show that he made payments in these amounts in 2009. As a result, the taxpayer's evidence is insufficient to support his burden to show that either of these two expenses is allowable. Accordingly, the Division properly disallowed the $$$$$ fee expense and the $$$$$ seminar expense.

81. TAXPAYER-1 testified that he paid for the $$$$$ BUSINESS-2 seminar and $$$$$ BUSINESS-3 seminar with credit cards. However, he admits that he does not have the credit card receipts to submit at the Formal Hearing. RESPONDENT stated that he had seen the credit card receipt in the amount of

44 Exhibit R-13 and P-8.

$$$$$ that TAXPAYER-1 paid to BUSINESS-2. RESPONDENT pointed out, however, that this credit card receipt did not show what the $$$$$ payment to BUSINESS-2 was for. RESPONDENT also stated that he had not seen a credit card receipt in the amount of $$$$$ that TAXPAYER-1 claims to have paid to BUSINESS-3.

82. BUSINESS-2. TAXPAYER-1 testified that he purchased the BUSINESS-2 seminar because it taught its students how to buy real estate online. He stated that the program he purchased also gave him access to manuals and a personal instructor who would call and provide personal assistance. To support his claim that he purchased this program, TAXPAYER-1 submitted enrollment and contact information that he and his wife received from BUSINESS-2. These documents describe the program that TAXPAYER-1 purchased as "NAME-9 Real Estate Program."[45]

83. The BUSINESS-2 information that TAXPAYER-1 submitted includes an "Enrollment Confirmation" letter that was addressed to both him and his wife. This letter is undated, but indicates that TAXPAYER-1 purchased 15 one-on-one sessions with a NAME-9 coach, access to "hotline advisors," access to property from over 5,000 lists before they go to auction, foreclosure training, access to software to enable him to locate distressed properties in the United States, the right to attend a two-day seminar with NAME-9 and/or staff, access to a tax coaching session, and different real estate guides and CD-ROMs.[46]

84. The Enrollment Confirmation letter indicates that it includes "a breakdown of your tuition." Immediately after this statement, however, was a description of the various training programs and/or products that have already been described in the prior paragraph. No information about the amounts of fees or tuition charged for each of these services and/or programs or even the total charges was included on the Enrollment Confirmation letter that TAXPAYER-1 submitted.

85. The Division admits that seminars and training TAXPAYER-1 may have purchased for his

45 Exhibit P-8.

real estate business would be an allowable expense. There is also no dispute that TAXPAYER-1 paid $$$$$ to NAME-9. The Division, however, asks the Commission to consider that the $$$$$ credit card receipt it saw (which neither party submitted as evidence) did not show what the $$$$$ payment was for and, as a result, did not show that it was for the training and other services and/or products described in the Enrollment Letter. In addition, the Division points out that the Enrollment Letter does not show the price TAXPAYER-1 paid for the services and/or products he purchased. The Division contends that it must see evidence that directly ties the $$$$$ payment to the services and/or products described in the Enrollment Letter before the payment should be allowed as an expense.

86. The Division also asked TAXPAYER-1 about a complaint filed against BUSINESS-2 in which NAME-9 was ordered to pay $$$$$ to consumers. TAXPAYER-1 stated that he was not familiar with any complaint against BUSINESS-2 and NAME-9 concerning the services and/or products he purchased from them. RESPONDENT also stated that the information is insufficient to show whether TAXPAYER-1 was purchasing education or products from BUSINESS-2. However, he admitted that purchasing a product such as a list of properties for a real estate business would be an allowable expense.

87. As the Division points out, TAXPAYER-1 has not provided a document showing that the services and/or products described in the NAME-9 Enrollment Letter are the ones for which he made his $$$$$ payment to NAME-9. As a result, there remains some question about the purpose of the $$$$$ payment. However, a preponderance of the evidence supports the taxpayer's claim that he made this $$$$$ payment to receive real estate training, services, and products for his real estate business. The items the taxpayer purchased are detailed on the Enrollment Confirmation letter, and the list of items is extensive. It does not seem implausible that such a program could cost the $$$$$ amount that TAXPAYER-1 is known to have paid NAME-9. There is no evidence to suggest that TAXPAYER-1 purchased something from NAME-9

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46 Exhibit P-8.

that would not be an allowable deduction. For these reasons, the taxpayer has proffered sufficient evidence to show that the $$$$$ seminar expense he claimed on Schedule C of his 2009 federal return should be allowed.

88. BUSINESS-3. TAXPAYER-1 testified that he attended a free seminar that BUSINESS-3 held in CITY-1, Utah. He testified, however, that to participate in the real estate opportunities they had, he had to become a member of BUSINESS-3. As a result, he contends that he paid $$$$$ to become a member of BUSINESS-3 and to obtain access to their program, which included access to a list of distressed properties in which he could invest. To support his claim that he paid $$$$$ to become a BUSINESS-3 member and participate in their program, TAXPAYER-1 submitted portions of a (X) Real Estate Manual that he received from BUSINESS-3. The manual indicates that "[e]ach member is assigned to a Personal Advisor who will be your point of contact at BUSINESS-3. Your PA is trained to answer your questions, notify you of upcoming events, and help you make appointments with your coaches."[47]

89. For this expense, the Division did not admit to having seen a credit card payment equal to the $$$$$ amount that TAXPAYER-1 claimed as an expense. In addition, TAXPAYER-1 has not provided evidence of this receipt or any document that would show he paid $$$$$ to BUSINESS-3. While it appears that TAXPAYER-1 probably paid some amount to BUSINESS-3 to become a member and to have access to its programs and a personal advisor, there is no documentary evidence to support his claim that this payment amounted to $$$$$. Without such evidence, a preponderance of the evidence does not support allowing this particular expense. As a result, the Division's disallowance of the $$$$$ seminar expense should be sustained.

90. Summary – "Other Expenses". Based on the foregoing, the taxpayer has submitted sufficient evidence to only support $$$$$ of the $$$$$ of "other expenses" that he deducted on his 2009 Schedule C. The taxpayer has not submitted sufficient evidence to support the remaining $$$$$ of the "other expenses." As a result, $$$$$ of the Division's disallowance of "other expenses" should be sustained and the remainder of

47 Exhibit P-8.

the disallowance should be reversed.

Issue 9: Cash Contributions – 2011 Tax Year

91. For the 2011 tax year, the Division disallowed a portion of the charitable cash contribution that the taxpayer had claimed on his 2011 federal return. Specifically, the Division disallowed $$$$$ of the deduction.[48] This is the second of two items on the Division's 2011 assessment that the taxpayer is contesting (the other item was previously addressed in Issue 5). The Division admits that the IRS accepted the taxpayer's 2011 federal return and has not audited the charitable cash contribution deduction he claimed for this year.

92. On Schedule A of his 2011 federal return, TAXPAYER-1 claimed an itemized deduction for charitable cash contributions in the amount of $$$$$.[49] The Division disallowed $$$$$ of this deduction, but allowed the remaining $$$$$.

93. At the Formal Hearing, the taxpayer asked to be allowed to submit evidence to show that the Division's disallowance of $$$$$ of the deduction was incorrect, even though he had not raised this issue by the June 23, 2015 deadline the Commission established in its March 27, 2015 Order Granting Petitioner's Continuance Request and Second Formal Hearing Scheduling Order. (This was also not an issue that was raised and addressed at the Initial Hearing). Specifically, the taxpayer asked to submit an Annual Charitable Cash Contributions Official Tax Summary Statement document from his church showing that he made donations in 2011 that totaled $$$$$.[50]

94. The Division stated that the church statement is adequate evidence to show that the taxpayer was entitled to claim an itemized deduction for charitable cash contributions of $$$$$. Nevertheless, the Division objected to the Commission allowing the taxpayer to raise this issue at the Formal Hearing for two

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48 Exhibit R-17.
49 Exhibit R-19.
50 Exhibit P-6.

reasons, the first being that the taxpayer did not raise the issue by the June 23, 2015 deadline set forth in the scheduling order, as discussed in the previous paragraph. Second, the Division stated that it had relied on a July 28, 2015 Order Concerning Respondent's Request for Default and Dismissal, and Prehearing Brief ("July 28, 2015 Order"), in which the Commission had denied the Division's July 14, 2015 request for the Commission to default the taxpayer and dismiss his appeal. In its July 28, 2015 Order, the Commission specifically ruled, as follows in pertinent part:

> . . . the taxpayer will not be allowed to raise issues at the upcoming Formal Hearing that he did not identify on or before the June 23, 2015 deadline set forth in the Commission's scheduling order. As a result, the taxpayer will not be allowed to raise the charitable cash contributions issue he identified in his July 17, 2015 letter, unless he also identified this issue in a document he submitted on or prior to June 23, 2015.[51]

95. At the Formal Hearing, the taxpayer did not assert that he had raised the charitable cash contribution issue on or before the June 23, 2015 deadline set forth in the Commission's scheduling order. The taxpayer pointed out, however, that the Commission's scheduling order only indicated that the 2005 through 2010 tax years were at issue, thus omitting the 2011 tax year for which the charitable cash contribution issue applies. After considering this point, the Commission decided at the hearing to allow the taxpayer to raise this issue because of due process concerns. So that the Division would not be disadvantaged, the Commission allowed the Division 10 days to respond in writing to this issue and to the church statement the taxpayer submitted as evidence. The Division did not respond.

96. The only evidence of TAXPAYER-1's 2011 charitable cash contributions is the church statement that shows that he made $$$$$ of contributions in 2011. This evidence is sufficient to support $$$$$ of the $$$$$ itemized deduction for charitable cash contributions that TAXPAYER-1 claimed for 2011. TAXPAYER-1, however, did not provide any evidence to support the remaining $$$$$ of the deduction he

51 Before the Commission issued an order ruling on the Division's July 14, 2015 request for default and dismissal of the taxpayer's appeal, the taxpayer submitted a response to the Division's request. With his response, the taxpayer raised the charitable cash contribution issue and submitted the church statement

claimed for 2011 ($$$$$ minus $$$$$). Accordingly, TAXPAYER-1's evidence is sufficient to show that the Division's charitable deduction disallowance of $$$$$ should be reduced to $$$$$. This has the effect of reversing $$$$$ of the $$$$$ amount that the Division disallowed ($$$$$ minus $$$$$).

APPLICABLE LAW

UTAH LAW.

1. Utah Code Ann. §59-10-104(1) (2011)[52] provides that ". . . a tax is imposed on the state taxable income of a resident individual as provided in this section."

2. For the 2005 and 2006 tax years only, UCA §59-10-112 (2006) (since repealed) defined "state taxable income" to mean "federal taxable income (as defined by Section 59-10-111) with the modifications, subtractions, and adjustments provided in §59-10-114;" and UCA §59-10-111 (2006) (since repealed) defined "federal taxable income" to mean "taxable income as currently defined in Section 63, Internal Revenue Code of 1986."[53]

3. For the 2007 through 2011 tax years, the terms "adjusted gross income," "federal taxable income," and "'taxable income' or 'state taxable income'" are defined in UCA §59-10-103 (2011), as follows in pertinent part:

> (1) As used in this chapter:
> (a) "Adjusted gross income":
> (i) for a resident or nonresident individual, is as defined in Section 62, Internal Revenue Code; . . .
> . . . .
> (f) "Federal taxable income":
> (i) for a resident or nonresident individual, means taxable income as defined by Section 63, Internal Revenue Code; . . .
> . . . .

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showing $$$$$ of 2011 contributions.

52 The 2011 version of Utah law is cited in the decision, unless otherwise indicated. Section 59-10-104(1) was amended in 2008, but throughout the tax years at issue, this provision provided that tax is imposed on the "state taxable income" of a resident individual.

53 Beginning with the 2007 tax year, these definitions are found in Section 59-10-103. The changes between the 2006 and 2007 law in regards to these definitions do not impact this decision.

(w) "Taxable income" or "state taxable income":[54]
(i) . . . for a resident individual, means the resident individual's adjusted gross income after making the:
(A) additions and subtractions required by Section 59-10-114; and
(B) adjustments required by Section 59-10-115; . . .
. . . .

4. Utah Admin. Rule R865-9I-18 ("Rule 18")[55] provides that a taxpayer will keep income tax records, as follows:

> A. Every taxpayer shall keep adequate records for income tax purposes of a type which clearly reflect income and expense, gain or loss, and all transactions necessary in the conduct of business activities.
> B. Records of all transactions affecting income or expense, or gain or loss, and of all transactions for which deductions may be claimed, should be preserved by the taxpayer to enable preparation of returns correctly and to substantiate claims. All such records shall be made available to an authorized agent of the Tax Commission when requested, for review or audit.

5. UCA §59-1-1417(1) (2015) provides that the burden of proof is upon the petitioner in proceedings before the Commission, with limited exceptions as follows:

> (1) In a proceeding before the commission, the burden of proof is on the petitioner except for determining the following, in which the burden of proof is on the commission:
> (a) whether the petitioner committed fraud with intent to evade a tax, fee, or charge;
> (b) whether the petitioner is obligated as the transferee of property of the person that originally owes a liability or a preceding transferee, but not to show that the person that originally owes a liability is obligated for the liability; and
> (c) whether the petitioner is liable for an increase in a deficiency if the increase is asserted initially after a notice of deficiency is mailed in accordance with Section 59-1-1405 and a petition under Part 5, Petitions for Redetermination of Deficiencies, is filed, unless the increase in the deficiency is the result of a change or correction of federal taxable income:
> (i) required to be reported; and

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54 For the 2007 tax year, this subsection provided that the "taxable income" or "state taxable income" of a resident individual meant "federal taxable income" (not "adjusted gross income" as reflected in the 2008 through 2011 law) after making the additions, subtractions, and adjustments of Sections 59-10-114 and 59-10-115. The change between the 2007 and 2008 law in regards to this definition does not impact this decision.

55 This rule remained the same during the tax years at issue until late 2011 when it was renumbered and when minor, non-substantive amendments were made to it. These changes do not impact this decision. It is also noted that beginning in 2009, Utah Code Ann. §59-1-1406(1) also requires a person to keep books and records that are necessary to determine the amount of a tax, fee, or charge to which he or she is subject.

(ii) of which the commission has no notice at the time the commission mails the notice of deficiency.

INTERNAL REVENUE CODE.

6. IRC §108 (2005) provides that certain discharges of indebtedness may be excluded from gross income, as follows in pertinent part:

(a) Exclusion from gross income
(1) In general
Gross income does not include any amount which (but for this subsection) would be includible in gross income by reason of the discharge (in whole or in part) of indebtedness of the taxpayer if—
. . . .
(B) the discharge occurs when the taxpayer is insolvent,
. . . .
(3) Insolvency exclusion limited to amount of insolvency
In the case of a discharge to which paragraph (1)(B) applies, the amount excluded under paragraph (1)(B) shall not exceed the amount by which the taxpayer is insolvent.

(b) Reduction of tax attributes
(1) In general
The amount excluded from gross income under subparagraph . . . (B) . . . of subsection (a)(1) shall be applied to reduce the tax attributes of the taxpayer as provided in paragraph (2).
(2) Tax attributes affected; order of reduction
. . . , the reduction referred to in paragraph (1) shall be made in the following tax attributes in the following order:
(A) NOL . . . .
(B) General business credit . . . .
(C) Minimum tax credit . . . .
(D) Capital loss carryovers . . . .
(E) Basis reduction
(i)In general
The basis of the property of the taxpayer.
. . . .
(F) Passive activity loss and credit carryovers . . . .
. . . .

(d) Meaning of terms; special rules relating to certain provisions
. . . .
(3) Insolvent
For purposes of this section, the term "insolvent" means the excess of liabilities over the fair market value of assets. With respect to any discharge, whether or not the taxpayer is insolvent, and the amount by which the taxpayer is insolvent, shall be determined on the basis of the taxpayer's assets and liabilities immediately before the discharge.

. . . .

7. IRC §165 (2006) provides that certain losses may be allowed as a deduction from income for tax purposes, as follows in pertinent part:

> (a) General rule
> There shall be allowed as a deduction any loss sustained during the taxable year and not compensated for by insurance or otherwise.
> . . . .
> (c) Limitation on losses of individuals
> In the case of an individual, the deduction under subsection (a) shall be limited to—
> (1) losses incurred in a trade or business;
> (2) losses incurred in any transaction entered into for profit, though not connected with a trade or business; and
> (3) except as provided in subsection (h), losses of property not connected with a trade or business or a transaction entered into for profit, if such losses arise from fire, storm, shipwreck, or other casualty, or from theft.
> . . . .
> (e) Theft losses
> For purposes of subsection (a), any loss arising from theft shall be treated as sustained during the taxable year in which the taxpayer discovers such loss.
> . . . .

DISCUSSION

The taxpayer contests a number of the changes the Division made to his Utah returns in its assessments for the years at issue. In accordance with Section 59-1-1417(1), the taxpayer has the burden to show that the Division's actions were incorrect. However, before addressing each of the contested issues, the Commission will first address the taxpayer's concern that changes should not be made to items reported on his Utah returns if the same items were reported on his federal returns and have not been changed by the IRS.

The Commission has heard a number of cases where a taxpayer asks the Commission to make an independent determination for an item on his or her Utah return that is not reflected on the taxpayer's federal return as shown in IRS records. In these cases, the Division often asks the Commission to reject a change for Utah tax purposes unless the IRS is willing to make the corresponding change at the federal level. Nevertheless, the Commission has, on occasion, made an independent determination regarding a person's

federal taxable income, even though the same determination has not been made by the IRS. For example, in *USTC Appeal No. 06-1408* (Initial Hearing Order, Nov. 5, 2007),[56] the Commission explained its willingness to make an independent determination in certain circumstances, as follows:

> The Utah Code sections specify that state taxable income is federal taxable income as defined in the Internal Revenue Code, (sic) they do not tie the state taxable income to the federal taxable income as determined by the IRS. Certainly the Tax Commission will give great deference in the interpretation of the Internal Revenue Code to the IRS, as they are the experts in this area. However, where there is a clear error and the taxpayer was unable to have the merits reviewed by the IRS due to the statute of limitations or for other procedural reasons, the Commission concludes that it is appropriate to give consideration to the definitions provided in the Internal Revenue Code.

In the instant case, there is no reason for the taxpayer to ask the IRS to add income or remove an expense or deduction where the IRS appears to have accepted the federal returns and where the taxpayer believes his federal returns are correct. In addition, there is no evidence to suggest that the Division can ask the IRS to review items reported on or left off the taxpayer's federal returns. As a result, it does not appear that the changes made by the Division in its audit are items likely to be reviewed by the IRS. Furthermore, Rule 18(B) requires a taxpayer to make records concerning income, expenses, and deductions available to an authorized agent of the Tax Commission upon request, which suggests that the Division can review and, if necessary, make changes for state tax purposes to an item that appears on both a taxpayer's federal and Utah returns. For these reasons, the Commission should make an independent determination of whether the taxpayer has met his burden to show that the contested changes that the Division made in its assessments are incorrect.

Issue 1: Income from Cancellation of Debt – 2005 Tax Year. IRC §108(a)(1)(B) provides that gross income does not include an amount which but for this subsection would be includable in gross income by reason of the discharge if "the discharge occurs when the taxpayer is insolvent." IRC §108(d)(3) defines

56 Redacted copies of this and other selected decisions can be viewed on the Commission's website at http://www.tax.utah.gov/commission-office/decisions.

"insolvent" to mean "the excess of liabilities over the fair market value of assets" and provides that the amount by which the taxpayer is insolvent "shall be determined on the basis of the taxpayer's assets and liabilities immediately before the discharge." Previously, the Commission has found that the taxpayer has not shown that he calculated his assets and liabilities and determined his net worth "immediately before the discharge."

In addition, even if the Commission were to consider December 31, 2005 as the date on which the taxpayer would need to show a negative net worth to qualify for the exclusion from income, the taxpayer's evidence is insufficient to show that he actually had a negative net worth on this date. Not only does it appear that the asset value of his personal residence needs to be increased by $$$$$, but it is also clear that $$$$$ needs to be added to his assets for a BANK-2 checking account. In addition, it appears that the taxpayer should have listed the $$$$$ transaction with COMPANY-2 as an asset before learning that the transaction may have been fraudulent the next year. Adding these amounts to the taxpayer's assets would result in his having a positive net worth as of December 31, 2005, which would also result in his not qualifying for the exclusion from taxation of the debt cancellation income.

Regardless of whether all of the amounts listed in the prior paragraph should be added to the taxpayer's assets, the taxpayer's failure to provide evidence of the value of his dental instruments and his other account balances is sufficient to sustain the Division's assessment of this item of income. The taxpayer did not provide evidence to show what the value of his dental instruments was as of December 31, 2005. In addition, he did not provide account statements to show the balance that existed for the other accounts he admitted to having. Without such evidence, the taxpayer has not shown that his Balance Sheet reflects all of his assets and, thus, has not shown that he qualifies for the exclusion from taxation of the debt cancellation income.

Lastly, the taxpayer did not file a Form 982 and did show that he reduced his tax attributes by the applicable amount, as required by IRC §108(b). For these various reasons, the taxpayer's evidence is

insufficient to show that he properly excluded from taxation the debt cancellation income at issue. Accordingly, the Division's assessment of tax on this income should be sustained.

Issue 2: Depreciation for VEHICLE-5 - 2007 Tax Year. Both parties agree that IRC §179 allows a small business to expense depreciable assets such as a VEHICLE-5. Both parties also agree that the $$$$$ depreciation expense claimed by TAXPAYER-1 may be appropriate if the mileages with which he calculated this amount are correct. To support his depreciation expense, TAXPAYER-1 reported that the VEHICLE-5 was driven a total of ##### miles in 2007 and that ##### of these miles were for a business purpose.

The Division argues that TAXPAYER-1's testimony and the limited documentary evidence he provided are insufficient to show that these mileages are correct. The Division's position is persuasive. TAXPAYER-1 did not provide the calendar on which he recorded these mileages when they occurred. He also did not provide an affidavit or other document from NAME-2 that would corroborate the conversation that he claims to have had with NAME-2. He also provided no gas receipts for the trip to CITY-2 or evidence showing that COMPANY-1 had built condominiums in CITY-2 that were similar to the ones he purchased in CITY-3. Given the lack of supporting documentary evidence, the Commission has found that the taxpayer did not meet his burden to show that the VEHICLE-5 was driven for ##### total miles in 2007 or that ##### of these miles were for a business purpose.

On the basis of this finding, the Commission also finds that the taxpayer has not met his burden to show that the $$$$$ depreciation expense he claimed for the VEHICLE-5 in 2007 was appropriate. Accordingly, the Commission should sustain the Division's disallowance of the entire $$$$$ depreciation expense in its assessment for the 2007 tax year.

Issue 3: Sale of a Cabin - 2007 Tax Year. Both parties agree that TAXPAYER-1 may deduct the cost of goods sold from the sales price of the cabin to determine his income from the sale. The issue, however, is whether TAXPAYER-1 has provided sufficient information to support the $$$$$ cost of goods sold amount

that he claimed in regards to the sale. The Division disallowed $$$$$ of this amount in its assessment, but could not explain how it determined this amount and why it had originally concluded that the remaining cost of goods sold amount that TAXPAYER-1 claimed should be allowed.

TAXPAYER-1's testimony that he and his son NAME-4 were partners in this enterprise was supported by documentary evidence. This evidence also supports most of the components that comprised the $$$$$ cost of goods sold amount that TAXPAYER-1 claimed on his federal return. It appears that NAME-4 reported his half of the cabin's sales price and costs when he reported his $$$$$ share of the profits from the cabin on his 2007 federal return. NAME-4's reported gain from the sale of the cabin and the cost amounts he reported to the IRS support all of the costs that comprised TAXPAYER-1's cost of goods sold amount with one exception. This evidence only supports $$$$$ of the $$$$$ of remodel costs that TAXPAYER-1 reported, but does not support the remaining $$$$$ of remodel costs that TAXPAYER-1 included in his cost of goods sold amount. For these reasons, the Commission should allow all but $$$$$ of the cost of goods sold amount that TAXPAYER-1 reported. Accordingly, the Division's 2007 assessment should be revised to reflect a disallowance of cost of goods sold for the cabin of only $$$$$.

Issue 4: Sale of a Recreational Lot – 2009 Tax Year. Both parties agree that TAXPAYER-1 may deduct the cost of goods sold from the sales price of the lot to determine his income from the lot sale. The issue, however, is whether TAXPAYER-1 has provided sufficient information to support the $$$$$ cost of goods sold amount that he claimed in regards to the sale. In its 2009 assessment, the Division disallowed $$$$$ of this amount because it had only seen three checks totaling $$$$$ that TAXPAYER-1 had paid to NAME-5. TAXPAYER-1, however, submitted a letter from NAME-5 in which she stated that she sold the lot to him for $$$$$. Based on a preponderance of the evidence standard, this evidence is sufficient to support the $$$$$ cost of goods sold amount that TAXPAYER-1 reported to the IRS. Accordingly, the Commission

should reverse that portion of the Division's 2009 assessment concerning its disallowance of $$$$$ of the cost of goods sold amount that TAXPAYER-1 reported to the IRS.

Issue 5: Mortgage Interest Deduction – 2009, 2010 and 2011 Tax Years. Both parties agree that a taxpayer may deduct interest paid on a second residence as an itemized deductions pursuant to IRC §163. Again, the issue is whether TAXPAYER-1 has provided sufficient evidence to support the interest deductions he claimed for his cabin in 2009, 2010, and 2011. The Commission has found by a preponderance of the evidence that the interest TAXPAYER-1 paid on the cabin amounted to $$$$$ for 2010, $$$$$ for 2011, and $$$$$ for 2011.

Accordingly, for 2009, that portion of the Division's assessment concerning the interest deduction should be revised to reflect a disallowance of only $$$$$. For 2010, that portion of the Division's 2010 assessment concerning the interest deduction should be reversed. For 2011, that portion of the Division's 2011 assessment concerning the interest deduction should be revised to reflect a disallowance of only $$$$$.

Issue 6: Mileage Deduction for Work Travel - 2008, 2009, 2010 and 2011 Tax Years (See Findings of Fact #64 and #65).

Issue 7: Investment Fraud Loss – 2006 Tax Year. For this issue, the parties disagree on whether TAXPAYER-1 has shown that he meets the legal requirements to qualify for an investment fraud theft loss under IRC §165. TAXPAYER-1 contends that he has provided sufficient information to show that he qualifies to take a theft loss of $$$$$ for the 2006 tax year based on the letters written by NAME-1. While these letters are sufficient to show that TAXPAYER-1 invested $$$$$ in 2004, they are not sufficient to show that he satisfied all requirements to claim a theft loss under IRC §165 and to deduct the $$$$$ amount at issue from his 2006 income.

Not only are the requirements to claim a theft loss set forth in IRC §165, but they are also discussed in the IRS's Publication 547, Casualties, Disasters, and Thefts (2006) ("Publication 547"). Publication 547 (p.

2) instructs a taxpayer who has a casualty or theft to report it by filing a Form 4684. TAXPAYER-1 filed a Form 4684 with his 2006 federal return and, thus, satisfied this requirement. However, the publication also indicates that to deduct a theft loss, "you must be able to show that there was a . . . theft" and "be able to show *all* the following" (emphasis added): 1) when you discovered that your property was missing; 2) that your property was stolen; 3) that you were the owner of the property; and 4) whether a claim for reimbursement exists for which there is a reasonable expectation of recovery. TAXPAYER-1 has not satisfied all of these requirements.

First, it is unclear when TAXPAYER-1 discovered that the $$$$$ was missing. His testimony on this fact was contradictory. The last statement he made concerning the timing of his discovery of the "theft" was that NAME-1 told him about the fraud before December 31, 2005. If this is true, it does not appear that TAXPAYER-1 qualifies to take a loss on his 2006 federal return. Not only does Section 165(a) provide for the loss "to be sustained during the taxable year," but Section 165(e) provides that a loss arising from theft "shall be treated as sustained during the taxable year in which the taxpayer discovers such loss." TAXPAYER-1 claimed the loss in 2006 but testified that he knew of the loss prior to 2006. Accordingly, it does not appear that he meets this requirement. Because TAXPAYER-1 does not meet this requirement, he does not qualify for the deduction at issue even if he meets all other requirements. However, as explained below, it does not appear that TAXPAYER-1 meets these other requirements.

Second, TAXPAYER-1 must show that his $$$$$ was stolen. Publication 547 (p. 2) and Rev. Rul. 72-112 both indicate that the taking of the property must be illegal under the jurisdiction where it occurred and that it must have been done with criminal intent. TAXPAYER-1 did not know where the taking of his $$$$$ occurred. Furthermore, other than NAME-1's and an unknown banker's assertion that fraudulent activities occurred, there is no evidence that a taking occurred that was illegal under the jurisdiction where it occurred and that it was done with criminal intent. The Commission has already found that these assertions are not

convincing because it is unknown whether either NAME-1 or the unknown banker is qualified to make legal conclusions concerning the legality of actions and criminal intent. Furthermore, there is no evidence to suggest that the FBI considered the action to be theft or prosecuted the alleged perpetrator after NAME-1 filed a complaint with them. Lastly, TAXPAYER-1 has provided few facts about the investment and the actions of the alleged perpetrator that could be applied to the applicable theft law, were that law known. For these reasons, TAXPAYER-1 has not proven that the $$$$$ was "stolen."

Third, TAXPAYER-1 has not shown that he was the owner of the money that the alleged perpetrators may have stolen. He has shown that he gave NAME-1 $$$$$ to invest. However, it is not known whether NAME-1 invested this money in COMPANY-3's name, TAXPAYER-1's name, or some other name. TAXPAYER-1 provided no details about the business relationship between himself and COMPANY-3. It is possible that TAXPAYER-1 invested in COMPANY-3 and COMPANY-3 invested in the entity that may have stolen the money. If so, it is arguable that COMPANY-3 was the owner of the money that was stolen, and TAXPAYER-1 was the owner of a different investment. Without more information, it is not clear that TAXPAYER-1 meets this requirement.

Fourth, the last requirement concerns whether a claim for reimbursement exists for which there is a reasonable expectation of recovery. Section 165(a) provides that a theft deduction is not allowable if the theft will be "compensated for by insurance or otherwise." Because TAXPAYER-1 did not address this requirement at the Formal Hearing, the Commission must find that he has not met his burden of proof to show that it is satisfied. Based on the foregoing, TAXPAYER-1 has not shown that he met all requirements necessary to claim the $$$$$ investment fraud theft loss that he deducted on his 2006 federal return.

Issue 8: Deductions for Training and Seminars – 2009 Tax Year. For the 2009 tax year, the Division disallowed $$$$$ of "other expenses" the taxpayer claimed on his 2009 Schedule C in regards to his real estate development business. TAXPAYER-1 showed that he reported to the IRS that the $$$$$ total

amount of "other expenses" consisted of four items, specifically a $$$$$ fee, an $$$$$ seminar, a $$$$$ seminar, and a $$$$$ seminar.

Because TAXPAYER-1 had no evidence to support the $$$$$ fee expense and the $$$$$ seminar expense, the Division's disallowance of these expenses should be sustained. As to the $$$$$ seminar expense, TAXPAYER-1 claimed that he paid this amount in order to become a member of BUSINESS-3 so that he could receive their training services and have access to their list of distressed properties. However, he provided no evidence to show that he made a payment in the amount of $$$$$ to BUSINESS-3. As a result, a preponderance of the evidence does not show that TAXPAYER-1 paid $$$$$ to BUSINESS-3. Accordingly, the Division's disallowance of the $$$$$ seminar expense should also be sustained.

As to the $$$$$ seminar expense, the evidence shows that TAXPAYER-1 made a payment in this amount to BUSINESS-2 (NAME-9). In addition, TAXPAYER-1 showed that he purchased a program from BUSINESS-2 that included a number of services and/or products. As a result, a preponderance of the evidence shows that TAXPAYER-1 paid $$$$$ to BUSINESS-2 for their program and supports his claiming this amount as an expense on his Schedule C. Accordingly, the Division's disallowance of this $$$$$ seminar expense should be reversed. In summary, $$$$$ of the Division's $$$$$ disallowance should be sustained, while the remaining $$$$$ of the disallowance should be reversed.

Issue 9: Cash Contribution – 2011 Tax Year. The parties disagreed on whether the taxpayer should even be allowed to raise this issue at the Formal Hearing. At the Formal Hearing, the Commission ruled that it would address the issue because it had omitted the 2011 tax year when it identified the tax years at issue on the Formal Hearing scheduling orders. So that the Division would not be disadvantaged, the Commission gave the Division an opportunity to submit a post-hearing response in regards to this issue. The Division did not submit a post-hearing response.

The evidence the Commission has received in regards to this issue is sufficient to support $$$$$ of the

$$$$$ itemized deduction for charitable cash contributions that TAXPAYER-1 claimed for 2011. TAXPAYER-1, however, did not provide any evidence to meet his burden of showing that he was entitled to deduct the remaining $$$$$. Accordingly, the Commission should reduce the Division's deduction disallowance by $$$$$, specifically from $$$$$ to $$$$$.

CONCLUSIONS OF LAW

1. In accordance with Section 59-1-1417(1), the burden of proof in this appeal is upon the taxpayer.

2. In accordance with Rule 18(B) and Commission precedent, the Division is authorized to investigate and assess tax on items that have been reported to the IRS and that the IRS has not audited and/or changed.

3. Issue 1: The taxpayer has not met his burden to show that he properly excluded from taxation the $$$$$of debt cancellation income at issue for the 2005 tax year. Accordingly, the Division's assessment of tax on this income should be sustained. Because this was the only item from the Division's 2005 assessment that the taxpayer contested, the Division's 2005 assessment should be sustained in its entirety.

4. Issue 2: The taxpayer has not met his burden to show that he qualifies to claim $$$$$ of depreciation expense for the 2007 tax year in regards to the VEHICLE-5 he purchased that year. Accordingly, the Division's disallowance of this expense on its 2007 assessment should be sustained.

5. Issue 3: The taxpayer has met his burden to show that he qualifies to claim all but $$$$$ of the cost of goods sold amount that he claimed for the 2007 tax year in regards to the 2007 sale of a cabin. Accordingly, the Division's disallowance of $$$$$ of the costs of goods sold that the taxpayer claimed should be reduced to $$$$$. Because this is the last item from the Division's 2007 assessment that the taxpayer contested, the Division's 2007 assessment should be sustained in its entirety with one exception. The Division should revise its 2007 assessment to reflect a disallowance of cost of goods sold for the cabin of only $$$$$.

6. Issue 4: The taxpayer has met his burden to show that he qualifies to claim the entire $$$$$ cost of goods sold amount that he claimed for the 2009 tax year in regards to the sale of a recreational lot. Accordingly, the Commission should reverse that portion of the Division's 2009 assessment concerning the cost of goods sold deduction that TAXPAYER-1 claimed for this lot.

7. Issue 5: The taxpayer has met his burden to show that he qualifies to claim all of the mortgage interest for his cabin that he reported in 2010 and most of the interest he reported in 2009 and 2011. For 2009, the Division's disallowance should be reduced from $$$$$ to $$$$$. For 2010, the Division's disallowance should be completely reversed. For 2011, the Division's disallowance should be reduced from $$$$$ to $$$$$. Because this is the only item from the Division's 2010 assessment that the taxpayer contested, the Division's 2010 assessment should be sustained except for reversing the disallowance of this mortgage interest deduction.

8. Issue 6: Because the taxpayer is no longer contesting the mileage deduction issue that was labeled "Issue 6" in the Initial Hearing Order, he is not contesting any portion of the Division's 2008 assessment. Accordingly, the Commission should sustain the Division's 2008 assessment in its entirety.

9. Issue 7: The taxpayer has not met his burden to show that he meets all of the requirements necessary to claim an investment fraud theft loss for the 2006 tax year. Accordingly, the Division's disallowance of the $$$$$ deduction claimed by the taxpayer should be sustained. Because this was the only item from the Division's 2006 assessment that the taxpayer contested, the Division's 2006 assessment should be sustained in its entirety.

10. Issue 8: In regards to the Division's disallowance of $$$$$ of Schedule C expenses for the 2009 tax year, the taxpayer has met his burden to show that $$$$$ of the disallowance should be reversed. However, the taxpayer has not met his burden to show that the remaining $$$$$ should be reversed. Accordingly, the Commission should sustain $$$$$ of the Division's disallowance, but should reverse the

remaining $$$$$. Because this is the last issue concerning the 2009 tax year, the Division's 2009 assessment should be sustained except that the Commission should: 1) completely reverse the Division's disallowance of the $$$$$ cost of goods sold deduction concerning the recreational lot (as discussed in Issue 4); 2) reduce the Division's $$$$$ disallowance of mortgage interest from $$$$$ to $$$$$ (as discussed in Issue 5); and 3) reduce the Division's disallowance of "other expenses" from $$$$$ to $$$$$.

11. Issue 9: In regards to the Division's disallowance of $$$$$ of charitable cash contributions, the taxpayer has met his burden to show that $$$$$ of the disallowance should be reversed. However, the taxpayer has not met his burden to show that the remaining $$$$$ of the disallowance should be reversed. Accordingly, the Commission should sustain $$$$$ of the Division's disallowance, but should reverse the remaining $$$$$. Because this is the last issue concerning the 2011 tax year, the Division's 2011 assessment should be sustained except that Commission should: 1) reduce the Division's $$$$$ disallowance of mortgage interest to $$$$$ (as discussed in Issue 5); and 2) reduce the Division's disallowance of charitable deductions from $$$$$ to $$$$$.

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Kerry R. Chapman
Administrative Law Judge

DECISION AND ORDER

Based on the foregoing, the Commission finds that the Division's 2005, 2006, and 2008 assessments should be sustained in their entireties.

The Division's 2007 assessment is sustained with one exception. The Division is ordered to revise the 2007 assessment to allow all but $$$$$ of the cost of goods sold amount of $$$$$, that the taxpayer claimed for the cabin he sold that year.

The Division's 2009 assessment should be sustained with three exceptions. The Division is ordered to revise the 2009 assessment to: 1) allow all of the cost of goods sold amount of $$$$$ that the taxpayer claimed in regards to the recreational lot; 2) allow all but $$$$$ of the mortgage interest that the taxpayer claimed as an itemized deduction; and 3) allow all but $$$$$ of the "other expenses" that the taxpayer claimed on his Schedule C.

The Division's 2010 assessment should be sustained with one exception. The Division is ordered to revise the 2010 assessment to allow all of the mortgage interest that the taxpayer claimed as an itemized deduction that year.

The Division's 2011 assessment should be sustained with two exceptions. The Division is ordered to revise the 2011 assessment to: 1) allow all but $$$$$ of the mortgage interest that the taxpayer claimed as an itemized deduction; and 2) allow all but $$$$$ of the charitable cash contribution that the taxpayer claimed as an itemized deduction. It is so ordered.

DATED this _____ day of _____, 2015.

John L. Valentine
Commission Chair

Michael J. Cragun
Commissioner

Robert P. Pero
Commissioner

Rebecca L. Rockwell
Commissioner

Notice of Appeal Rights: You have twenty (20) days after the date of this order to file a Request for Reconsideration with the Tax Commission Appeals Unit pursuant to Utah Code Ann. §63G-4-302. A Request for Reconsideration must allege newly discovered evidence or a mistake of law or fact. If you do not file a Request for Reconsideration with the Commission, this order constitutes final agency action. You have thirty (30) days after the date of this order to pursue judicial review of this order in accordance with Utah Code Ann. §§59-1-601et seq. and 63G-4-401 et seq.