

IN THE OREGON TAX COURT  
MAGISTRATE DIVISION  
Income Tax

LELAND J. GROSS,	)	
	)	
Plaintiff,	)	TC-MD 030951A
	)	
v.	)	
	)	
DEPARTMENT OF REVENUE,	)	
State of Oregon,	)	
	)	
Defendant.	)	<b>DECISION</b>

Plaintiff, a veterinary physician, appealed personal income tax assessments for the 1998 and 1999 tax years. A trial was held June 30, 2004. Plaintiff represented himself. Defendant appeared through its employee, Cecilia Beito.

I. STATEMENT OF FACTS

Plaintiff, a veterinarian with some 25 years of experience, operates the Corvallis Veterinary Hospital as a sole proprietorship. His income tax returns, particularly his Schedule C business expenses, were audited by Defendant. Tax to pay for the 1998 and 1999 tax years was \$2,637 and \$2,141 respectively, with additional interest and penalties.

Testimony about the veterinary hospital came from Plaintiff and Laura Jensen, his longtime employee. The business cares for the general health of small animals. It operates out of a building owned by Plaintiff, who also owns other rental properties. There are five employees.

On the 1998 return, Plaintiff's Schedule C shows gross receipts from the veterinary hospital of \$159,608, and supplies at \$92,007, with total business expenses of \$187,870, for a \$28,262 loss. In 1999, the gross receipts were \$146,490, supplies \$80,808, with \$183,381 in total business expenses, for a \$36,891 loss. Plaintiff's bookkeeping only ran to incoming accounts, day slips, and billing. Defendant's audit concluded that the expenses summarized on the returns appeared to be for personal, rather than business items.

Defendant's audit disallowed travel, meals, gasoline, auto supplies, groceries, and items purchased at department and discount stores. The effect of those adjustments was to reduce Plaintiff's Schedule C deduction for supplies to approximately two-thirds of their level as set out on the return, for a change in income of \$30,876 in 1998 and \$23,840 in 1999. Other adjustments followed to the self-employment tax and understatement penalty. Although Plaintiff admitted that some minor adjustments to the returns were proper, such as removing airline tickets in the amount of \$1,100 for 1998, and \$3,010 in tours and double entries for 1999, Plaintiff objected to the balance of the audit adjustments.

Plaintiff's argument was that all the expenses set out on the returns were business expenses. His reasoning was that they were segregated from personal expenses because the purchases had been made with a BankCard Services Alaska Airlines credit card designated by Plaintiff to be used exclusively for business purchases. Plaintiff went on to explain that items that would appear to be for personal use were purchased either for the treatment of animals, or used by way of employee benefits.

Plaintiff explained how a veterinary hospital works from the perspective that items which would appear to be for personal use, were applied in the treatment of animals. Power tools purchased from discount stores were used to rebuild countertops and repair turtle shells. Garbage bags, batteries, and battery chargers are needed. Cleaning requires fluids, paper towels, and sometimes even power washers. Some distressed small animals prefer canned peaches. Maintenance of landscaping at the clinic requires items from the garden store. The waiting room needs books and music. The business has vehicles for its use. Employees need changes of clothing. Plumbing, electrical work, auto maintenance, painting, and carpentry are done by Plaintiff and his staff.

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Plaintiff went on to explain that items which appeared to be personal in character were used by way of employee benefits. Plaintiff, as part of his plan of employee compensation, provides food, excursions, trips, gifts, occasional use of a car and motor home, and some medical and education payments to his staff.

## II. ANALYSIS

Plaintiff is very convincing when he describes how many ordinary household items purchased at retail stores are used daily, in great quantities, by a veterinary clinic. That is not especially remarkable. It is true of many businesses. More is required to support the deductions in the amount claimed than making that point. It is at the next stage, when Plaintiff asserts that all his deductions must be permitted because they were made with a credit card he designates for business use, that his presentation breaks down.

Plaintiff did not keep business records in the manner appropriate for an enterprise bringing in annual gross receipts on the order of \$150,000. All Plaintiff did was to maintain income accounts. There was no tracking of expenses. That is especially important when the items purchased are so equivocal in character that they might be put to either personal or business use. Reliable records would have made Plaintiff's case more substantial. Simply testifying that an expense is a proper deduction is no substitute for good record keeping, and that is what Plaintiff did when he said a purchase must have been for supplies because it was made with a particular credit card. There is evidence in the record that Plaintiff's system has its shortcomings, even from his own perspective. For 1998, Plaintiff admitted his expenses included personal airline tickets that ought not to have been claimed. For 1999, his claimed expenses included a pleasure tour he later agreed should not have been listed.

Moreover, Plaintiff's attitude demonstrates a fundamental misunderstanding of the ability to claim a deduction. Plaintiff's method of defending the returns was to consistently challenge

Defendant to demonstrate that an item was used by him for a personal use, and not for a business purpose. That is not what is required. Rather, Plaintiff has the burden of proving that a deduction is, in fact, allowable. ORS 305.427.<sup>1</sup> Plaintiff's proof was worse than disorganized and incomplete. As Plaintiff offered no exhibits for this proceeding, Plaintiff's proof was nonexistent.

Without records to support Plaintiff's deductions, what might Plaintiff have done to support his claim? One option might have been for Plaintiff to show that the disputed items must be for a business purpose, because there are the other, separate personal expenses Plaintiff made to support his lifestyle. However, Plaintiff did not show the purchases he made in addition to the disputed items to live in the manner he was accustomed. Instead, the court is left to conclude that from his other income, Plaintiff is able to operate a business at a loss and support himself. Although that is a possibility, the court finds it is more likely that the items asserted to be business expenses include a large component of Plaintiff's personal expenditures.

As to the remaining point, the court is also of the opinion that Plaintiff does provide benefits to his employees beyond their paychecks. As to whether that is ordinary and necessary, as is required by Internal Revenue Code section 162, is another question. It is much more controversial when benefits are provided in lieu of higher wages, as there are consequences to federal tax programs that use wages to calculate employer payments. The court will, in this and all other respects, support the conclusion of Defendant.

A final point is that there is no temptation for the court to reduce the tax on the reasoning that, although Plaintiff's records were woefully inadequate, some of the expenses must have been for business purposes or were otherwise consistent with the revenue laws. That was already done by Defendant, who at the audit level allowed a large amount for supplies. For 1998, Defendant

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<sup>1</sup>All references to the Oregon Revised Statutes (ORS) are to 2003.  
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allowed 66 percent of the deduction; rising to 70 percent for 1999. Those percentages, in the context of this particular appeal, are reasonable.

### III. CONCLUSION

Now, therefore,

IT IS THE DECISION OF THIS COURT that the appeal is denied.

Dated this \_\_\_\_\_ day of October 2004.

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SCOT A. SIDERAS  
MAGISTRATE

**IF YOU WANT TO APPEAL THIS DECISION, FILE A COMPLAINT IN THE REGULAR DIVISION OF THE OREGON TAX COURT, BY MAILING TO: 1163 STATE STREET, SALEM, OR 97301-2563; OR BY HAND DELIVERY TO: FOURTH FLOOR, 1241 STATE STREET, SALEM, OR. YOUR COMPLAINT MUST BE SUBMITTED WITHIN 60 DAYS AFTER THE DATE OF THE DECISION OR THIS DECISION BECOMES FINAL AND CANNOT BE CHANGED.**

**THIS DOCUMENT WAS SIGNED BY MAGISTRATE SCOT A SIDERAS ON OCTOBER 29, 2004. THE COURT FILED AND ENTERED THIS DOCUMENT OCTOBER 29, 2004.**