

IN THE OREGON TAX COURT  
MAGISTRATE DIVISION  
Income Tax

ROBERT MATUSZAK	)	
and JERRIE MATUSZAK,	)	
	)	
Plaintiffs,	)	TC-MD 060392C
	)	
v.	)	
	)	
DEPARTMENT OF REVENUE,	)	
State of Oregon,	)	
	)	
Defendant.	)	<b>DECISION</b>

Plaintiffs appeal Defendant’s adjustments to their 2002 personal income tax return. A telephone trial was held October 13, 2006. Plaintiff Robert Matuszak (Robert) appeared on behalf of himself and Jerrie Matuszak (Jerrie).<sup>1</sup> Allen Schweigert appeared on behalf of Defendant.

I. STATEMENT OF FACTS

Plaintiffs are married and filed a joint personal income tax return for the 2002 tax year. (Ptf’s Ex 1.) In 2002, both were employed by the Greater Albany Public School District (the District). Robert was employed as the principal of Oak Elementary School, and Jerrie was employed as a Reading Coach/Teacher at Sunrise Elementary School. (Ptf’s Exs 5, 9.)

As educators, Plaintiffs incurred expenses for work-related travel (mileage and lodging), cellular phone service, and purchases of motivational tools for students and staff such as snacks, treats, and stickers. (*See, e.g.*, Ptf’s Exs 3, 11, 12, 20, 21.) Plaintiffs also incurred job search expenses related to Jerrie’s search for an administrative position. (*See* Ptf’s Exs 34, 35.)

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<sup>1</sup> For ease of reference, Plaintiffs will be referred to collectively as Plaintiffs and individually as Robert and Jerrie.

Plaintiffs kept detailed records of their expenses, including separate tax journals, which were submitted to the court. (*See* Ptf's' Exs 11, 12, 20, 21.)

A. *Employee Expense Allowances and Reimbursements*

Plaintiffs submitted evidence documenting employee reimbursement by schools in the District generally and of themselves individually. (*See* Ptf's' Exs 5, 6, 7, 8, 9, 10.) As an example of the limits placed on employee reimbursements in the District, Plaintiffs submitted part of the Oak Elementary School Staff Handbook from 2002-2003, which states under "Supplies" that "[e]ach classroom teacher [has] an allocation of \$125.00 to use towards supply items that are not normally carried by the school. Funds are contingent on district resources." (Ptf's' Ex 6 at 2.) Robert testified that "normally carried" supplies are items such as pens, paperclips, glue, and paper, but that the schools do not provide all of the necessary supplies to conduct class or run an administrative office. As the principal of Oak Elementary, Robert was responsible for developing the school budget, which "include[d] allocating funds \* \* \* and approving or denying reimbursements for employee expenses pertaining to his school." (Ptf's' Ex 5.) Robert explained that, although his principal's office had access to such normally carried supplies, any supplies needed for the principal's office beyond that were purchased out-of-pocket because the school's budget for 2002 did not allocate the principal's office any money for supplies. (*See* Ptf's' Ex 7.)

As an administrator, Robert worked under the "Administrative Confer and Consult Agreement,"<sup>2</sup> which provides him an expense allowance of \$100 per month (for 11 months annually). (Ptf's' Exs 5, 8; Def's Ex B at 1, 2.) Robert testified that this amount was for minor

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<sup>2</sup> Both parties submitted copies of the "2003/04 – 2005/06 Administrative Confer and Consult Agreement." There is no dispute, however, that the reimbursement amounts referenced therein also apply to the 2002 tax year.

expenses and local travel (within a 50 mile radius). (Ptf's Exs 5, 8; Def's Ex B.) Robert testified that he was required to have a cell phone and received a \$20 per month cellular phone allowance (for 11 months annually). (See Ptf's Ex 8 at 3.) Because Robert's expense allowances were taxed to him as income, Robert testified that he deducted the amounts paid for those items. (See Ptf's Ex 5.) Robert further testified that he did not submit for reimbursement expenditures falling within these allowances. When his business expenditures exceeded the allowance amount, he treated them as out-of-pocket expenses and deducted them as miscellaneous expenses. A letter from Robert's supervisor, the Assistant Superintendent, states that "[w]ith limited resources the district cannot reimburse all employee expenses." (Ptf's Ex 5.)

Robert was also allocated \$350 annually for administrative staff development, which included travel (outside the 50 mile local radius), meals, and lodging. Expenses incurred beyond \$350 were his responsibility. (See Ptf's Ex 5.) Robert testified that because the \$350 was not taxed as income, he did not claim a deduction for anything covered by that \$350.

Jerrie's expense allowance was also limited. Plaintiffs submitted a letter from Jerrie's current supervisor, the principal of Sunrise Elementary School, which states the "classroom reimbursements are limited to \$100 per teacher." (Ptf's Ex 9.) Robert clarified during the trial that this is an annual allowance. The letter further explains that "[w]ith limited resources the school cannot reimburse all employee expenses," and goes on to say that "[m]ost teachers spend their own money for ordinary and necessary supplies beyond what they receive in reimbursement. These items include student incentives, student supplies, books, etc." (*Id.*)

To further demonstrate the limits placed on reimbursement in the District, though not specifically in 2002, Plaintiffs submitted a letter from the former principal of Sunrise Elementary School. (Ptf's Ex 10.) The letter states that, in 2001, "Jerrie purchased a substantial amount of

supplies to assist in the instruction of the students she served. These expenditures for classroom supplies are a common occurrence for many teachers and are a vital part of the teaching profession.” (Ptf’s Ex 10.) (Emphasis in original.) The letter specified that Jerrie was reimbursed \$418.72 for expenses she incurred, but that “[t]his was only a portion of her total purchases[.]” and that, “[d]ue to a limited budget, Jerrie did not have the option to request additional reimbursement.” (*Id.*) (Emphasis in original.)

The District *currently* has an expense reimbursement policy (the Policy) which states, in part, that “[d]istrict employees who incur expenses in carrying out their authorized duties will be reimbursed upon submission of a properly completed and approved voucher and receipts as required by the business office[.]” and that “[s]uch expenses may be incurred and approved in line with budgetary allocations for specific types of expenses.” (Ptf’s Ex 4; Def Ex A at 6.)

Robert testified that the Policy was adopted December 8, 2003, and currently applies to Plaintiffs, but that it did not exist during the 2002 tax year. Plaintiffs are not aware of any other policy for 2002. Exhibits submitted by both parties show the adoption date of the Policy as “12/8/03.” (Ptf’s Ex 4; Def’s Ex A at 6.)

#### B. *Deductions*

On their 2002 personal income tax return, Plaintiffs claimed miscellaneous itemized deductions totaling \$7,573 and deductions for charitable contributions totaling \$2,156. (Ptf’s Ex 1 at 3.) Defendant issued a Notice of Deficiency (the NOD) on April 6, 2006, denying the charitable contributions and reducing the miscellaneous business deductions. Prior to trial, Plaintiffs submitted information that substantiated their claim for charitable contributions.

Defendant accepts Plaintiffs’ information; as a result, the charitable contributions are no longer at issue.

Plaintiffs submitted a list of their miscellaneous deductions totaling \$7,934, an increase of \$361 from the return as filed. (Ptf's Ex 3.) Robert testified that the increase is due to calculation errors on the return. Plaintiffs claim miscellaneous itemized deductions for business expenses, miles, travel, and job searches, as well as several other items that are not contested. (See Ptf's Ex 3.) Specifically, Robert had business expenses for school and office supplies (\$2,288), for lodging on business trips beyond what was reimbursed (\$30), and for business mileage (\$1,614 or 4,422 miles at \$.365/mile). (Ptf's Exs 3, 20.) Jerrie had business expenses for student and staff supplies and incentives (\$2,769), for meals (\$63 or \$125 x .5), and for business mileage (\$449 or 1,229 miles at \$.365/mile). (Ptf's Exs 3, 11.) Jerrie also had job search expenses for mileage (\$1,860 or 5,096 miles at \$.365/mile), for lodging (\$227), and for meals (\$270 or \$540 x .5). (Ptf's Exs 3, 34.)

In substantiation of their business expenses, Plaintiffs submitted individual tax journals with notations regarding expenditures, travel, and mileage. (See Ptf's Exs 12, 21.) Robert testified he and Jerrie updated their tax journals at or near the time of the expense. Plaintiffs also submitted cross-referenced spreadsheets of their 2002 business expenses (Ptf's Exs 11, 20), duplicate checks and expenditure receipts (Ptf's Exs 16, 22, 23), credit card, checking account, and banking ledgers (Ptf's Exs 14, 15, 17, 18, 19, 24, 25), and cellular telephone bills (Ptf's Exs 26, 27).

Robert testified that snacks, treats, cards, stickers, and classroom parties are motivational tools that increase student and staff performance and aid in behavior management. In support of Robert's testimony, Plaintiffs submitted excerpts from educational literature and articles that state positive rewards can be used effectively in the classroom. (See Ptf's Exs 29, 30, 31.) Relevant statements from those submissions include: "[M]ost children respond favorably to

rewards and incentives \* \* \*. Rewards can include a 15-minute party for good overall classroom behavior, individual stickers, paper money, points, and stars.”; “[P]ositive consequences that so motivate students” include “[s]pecial awards,” “[m]aterial rewards - - posters, school pencils, popcorn,” and “[g]roup rewards \* \* \*.” (Ptfs’ Ex 29 at 2; Ptfs’ Ex 30 at 4.)

To substantiate Jerrie’s job search expenses, Robert testified that she received her administrator’s license in 2001. Since then, Jerrie has been aggressively searching for an administrator’s job and Plaintiffs plan to relocate to wherever she finds a position. In addition to Jerrie’s tax journal, Plaintiffs submitted a ledger of expenses, receipts, and newspaper clippings advertising openings for school administrator positions. (*See* Ptfs’ Exs 12, 34, 35.) Robert testified that the trips to San Bernadino and Santa Rosa, California, were primarily for Jerrie to look for an administrator’s position and that all of the dates listed for those trips in her tax journal were primarily used for the job search. (*See* Ptfs’ Exs 12, 34.) At trial, Robert explained that the most effective job application process, which Jerrie used in 2002, is to go to a school district and do a “drop-in face-to-face” to talk to the people, give them a resume, show them you are interested in that area, then submit applications. Robert testified that, when visiting California, Jerrie looked over the entire San Bernadino and Santa Rosa areas for jobs and made daily visits to different district offices.

Defendant’s position is that Plaintiffs’ “Employee Business Expenses have been disallowed because the plaintiff[s’] employer \* \* \* has an accountable reimbursement plan. \* \* \* In addition to [the Policy], the employee contracts that the plaintiff’s [*sic*] fall under offer reimbursement of expenses incurred while conducting business.” (Def’s Answer at 1.) “Under [the Policy], the employee is reimbursed for all business related expenses; therefore the plaintiff[s] should have no un-reimbursed business related expenses.” (Def’s Answer at 1.)

Defendant also reduced Plaintiffs' job search expenses due to a lack of substantiation. (*See* Def's Answer at 2; Ptf's' Ex 2 at 3.)

Plaintiffs contend that the Policy is not applicable to the 2002 tax year and that, even had the Policy existed in 2002, the requirement that expenses "may be incurred and approved in line with budgetary allocations for specific types of expenses[ ]" makes it impossible to control what expenses are reimbursed. (Ptf's' Ex 4.) Robert testified that the District has limited funds to reimburse employees for job-related expenses and that the schools do not provide all of the necessary teaching and administrative tools or supplies. Plaintiffs further submitted information to substantiate their claimed expenses.

## II. ANALYSIS

The State of Oregon has adopted the federal definitions pertaining to taxable income as the measure of a taxpayer's Oregon taxable income. ORS 316.048.<sup>3</sup> The Internal Revenue Code (IRC) allows a deduction for "all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business." IRC § 162(a).<sup>4</sup>

A. *Were the claimed expenses "ordinary and necessary" under IRC section 162(a)?*

IRC section 162(a) states that expenses which are "ordinary and necessary expenses \* \* \* in carrying on any trade or business" are deductible. In contrast, "personal, living, or family expenses" are not deductible. IRC § 262(a). "To be 'necessary' an expense must be 'appropriate and helpful' to the taxpayer's business. \* \* \* To be 'ordinary[,] the transaction which gives rise to the expense must be of a common or frequent occurrence in the type of

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<sup>3</sup> All references to the Oregon Revised Statutes (ORS) are to 2001.

<sup>4</sup> All references to the IRC are to 2000.

business involved.” *Boyd v. Commissioner*, 83 TCM (CCH) 1253, 2002 WL 236685 at \* 2 (US Tax Ct) (*Boyd*) (internal citations omitted). This court has stated that “\* \* \* an ordinary expense is one which is customary or usual. This does not mean customary or usual within the taxpayer’s experience but rather in the experience of a particular trade, industry or community.” *Roelli v. Dept. of Rev.*, 10 OTR 256, 258 (1986) (*Roelli*) (citing *Welch v. Helvering*, 290 US 111, 54 S Ct 8, 78 L Ed 212 (1933)); *Guinn v. Dept. of Rev.*, TC-MD No 040472D, WL 1089727 at \* 4 (Apr 19, 2005) (citing *Roelli*, 10 OTR at 258).

Plaintiffs’ claimed deductions include expenditures for staff and student incentives. In addition to Robert’s testimony, Plaintiffs’ position that the expenditures are ordinary and necessary teaching and administrative tools is supported by the educational articles they submitted. (*See* Ptf’s Exs 29, 30, 31.) The evidence establishes that incentives are both motivational tools and behavior management aids which are appropriate and helpful to Plaintiffs’ profession and are commonly used throughout the educational community. The court agrees with Plaintiffs that the expenditures for incentives meet the IRC section 162(a) requirement of being “ordinary and necessary.”

Plaintiffs also had expenditures for school and office supplies. Robert testified that the schools provide limited types of items but do not provide all of the necessary supplies to conduct class or run an administrative office. The court finds that the school and office supply expenditures meet the definition of “ordinary and necessary” because the purchases were appropriate and helpful to, as well as a common or frequent occurrence in, Plaintiffs’ professions. *See* IRC § 162(a).

Similarly, the court finds that Plaintiffs’ expenses for travel, mileage, and Jerrie’s job search also meet the definition of “ordinary and necessary” under IRC section 162(a). The



evidence shows that the travel and mileage expenditures were directly related to either the jobs Plaintiffs had in 2002, or to Jerrie's search for an administrator's position in Oregon and California, that they were helpful and appropriate to those jobs, and that such activities and expenditures are a common occurrence in the industry.

B. *Were Plaintiffs required to seek reimbursement of the expenses?*

This court has recognized that "an expense is not 'necessary' under § 162(a) when an employee fails to claim reimbursement for the expenses, incurred in the course of his employment, when entitled to do so." *Symonds v. Dept. of Rev.*, 11 OTR 417, 418 (1990) (citing *Orvis v. Commissioner*, 788 F2d 1406, 1408 (9th Cir 1986) (*Orvis*)). This "bright line rule prohibiting deductions for reimbursable expenses avoids the difficult inquiry into the taxpayer's knowledge, and gives the taxpayer an incentive to determine which expenses are reimbursable. The rule also forecloses an avenue for tax manipulation by preventing the taxpayer from converting a business expense of his company into one of his own simply by failing to seek reimbursement." *Orvis*, 788 F2d at 1408.

Under that rule, Plaintiffs cannot deduct any amount for which they were entitled to seek reimbursement but failed to do so. It follows that Plaintiffs may take a miscellaneous itemized deduction for unreimbursed employee business expenditures for which they were *not* entitled to seek reimbursement.

Defendant points to the Policy as an accountable reimbursement plan and denied Plaintiffs' miscellaneous deductions because Plaintiffs failed to submit the expenses for reimbursement under the Policy. (*See* Def's Answer at 1.) However, written exhibits submitted by both parties, and Robert's testimony at trial, demonstrate the Policy was not adopted until December 8, 2003. (Ptf's Ex 4; Def Ex A.) Defendant did not submit any evidence to show the

Policy was adopted or effective in 2002. The court concludes that the Policy was not in effect in 2002 and is, therefore, not applicable in the present case.

Defendant also argues that Plaintiffs could have sought reimbursement for business expenses under their employment contracts. Plaintiffs' rights to seek reimbursement from their employer, however, were clearly limited. Jerrie's allowance for classroom expenses was \$100 annually and, according to Robert's testimony, she was not permitted to seek reimbursement for any amount. (*See* Ptf's' Ex 9.) Robert's monthly allowance for minor expenses and local travel was \$100, and his monthly cell phone allowance was \$20. (Ptf's' Ex 8.) Robert's right to seek reimbursement was limited to \$350 for travel, meals, and lodging related to administrative staff development. (Ptf's' Ex 5.) According to his testimony, Robert was reimbursed for his full \$350 allowance in 2002, although his expenses for an administrative development trip in June 2002 were \$380. (*See* Ptf's' Ex 28.) Plaintiffs claimed the additional \$30 as part of their miscellaneous itemized deductions. (*See* Ptf's' Ex 3.)

The evidence shows that Plaintiffs sought (and received) reimbursement for Robert's allocation of \$350, the only reimbursement they were entitled to seek. (*See* Ptf's' Ex 5.) Because Plaintiffs are not claiming deductions for any business expenses for which they were entitled to seek reimbursement, they are entitled to a miscellaneous itemized deduction for the full amount claimed, subject to sufficient substantiation under IRC section 274(d). That includes the allowance amounts received by Plaintiffs that were included in Plaintiffs' taxable income. Treas Reg § 1.62-2(c)(5).

### C. *Substantiation of Business Expenses*

Under IRC section 274(d), deductions under IRC section 162 are disallowed unless substantiated by "adequate records or by sufficient evidence corroborating the taxpayer's own

statement[.]” Even if an expense is otherwise deductible, the deduction may be denied if the information used to support the expense is insufficient. *See* Temp Treas Reg § 1.274-5T (as amended in 2003). Generally, the taxpayer is required to substantiate the expense amount, date and time, the business purpose, and the business relationship of the persons receiving gifts or entertainment. *See* IRC § 274(d). According to the NOD, Defendant reduced Plaintiffs’ deduction for job search expenses due to a lack of substantiation. (Ptf’s Ex 2 at 3.) Specifically, Defendant’s Answer states that Plaintiffs’ substantiation for Jerrie’s job search deductions “did not meet the substantiation requirements of IRC 274.” (Def’s Answer at 2.)

Plaintiffs argue their tax journals are adequate and timely kept records that are substantiated by their other exhibits and by Robert’s testimony. Robert testified that he and Jerrie updated their tax journals regularly and noted the amount of each expense at or near the time the expenditure was made. Plaintiffs provided a list of abbreviations used in their tax journals, cross-referenced tables of business expenses, and receipts. (*See* Ptf’s Exs 11, 16, 20, 23, 32, 33, 35.) In addition, Robert’s testimony regarding the methodology behind the evidence presented, the business purposes of the expenditures, and the business relationship with staff and students, further substantiates the expenses. With respect to Jerrie’s job search expenditures, Robert testified that all of the days listed in Jerrie’s tax journal as being spent on job search trips were primarily spent on her job search. (*See* Ptf’s Ex 12.) Plaintiffs also submitted receipts and newspaper clippings of job positions in Santa Rosa to substantiate her job search expenses for that trip. (*See* Ptf’s Ex 35.)

After considering and evaluating all the evidence provided by Plaintiffs, the court finds that Plaintiffs have met the substantiation requirements of IRC section 274(d) for their business

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expenses. Plaintiffs maintained daily journals and provided information to support the journal entries. The information clearly substantiates Plaintiffs' claimed expense deductions.

### III. CONCLUSION

The court concludes, based on the foregoing analysis, that Plaintiffs are entitled to a miscellaneous itemized deduction in the amount of \$7,939 for their ordinary and necessary business expenses. Based on Defendant's agreement, Plaintiffs are also entitled to the charitable deductions claimed on their 2002 federal tax return. Now, therefore,

IT IS THE DECISION OF THE COURT that Defendant shall cancel the Notice of Deficiency and recalculate the tax due, if any, in accordance with this Decision.

Dated this \_\_\_\_\_ day of March 2007.

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COYREEN R. WEIDNER  
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 Coyreen R. Weidner on March 20, 2007. The Court filed and entered this document on March 20, 2007.***