

TAX TALK
BY JEFFREY D. SKOLNICK, CPA, M.S. TAXATION

SUBSTANTIATION REQUIREMENTS

This article will focus on two of the more commonly contested deductions; automobile expense and meals and entertainment deductions.

What documentation do I need to deduct automobile expenses?

The first thing to keep in mind when deducting automobile expenses is that only business use is deductible. In previous articles I have addressed the two methods of deducting automobile expenses. The two methods are either actual costs or standard mileage rate. When using the actual costs method, the taxpayer as the term suggests, uses his or her actual costs of gas, insurance, depreciation, repairs, etc. These expenses are totaled and then allocated to either business or personal usage.

The standard mileage rate method simply applies the IRS standard rate (51 cents per mile from January 1, 2011 through June 30, 2011 and 55.5 cents per mile from July 1, 2011 through December 31, 2011) to the business mileage.

Keep in mind that under either method commuting mileage to and from the taxpayer's regular place of business is not considered business mileage.

The best way to substantiate business mileage is through the use of a diary. The IRS will want to see the date, mileage and business or investment purpose of each trip. When listing the business appointments it is important to note the location of each meeting. Listing the location will provide the auditor the information he/she needs to test whether the mileage shown is reasonable.

What documentation is needed to deduct meals and entertainment expenses?

The taxpayer must be able to show the amount, time and place and business purpose of each expense deducted as meals and entertainment. In addition, the taxpayer must be able to show the relationship to the taxpayer of persons entertained or receiving gifts.

Lastly, even when all of the above criteria are met only 50 % of meals and entertainment expenses are deductible.

What happens if I cannot substantiate expenses?

If deductions cannot be properly substantiated, the expenses would be disallowed and the taxpayer would likely be assessed an "accuracy-related" penalty of 20% of the tax balance due plus interest. If the IRS feels the expenses were fraudulent, then the penalties can be 75% of the additional tax amount due.

Conclusion

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This article discusses IRS positions on certain deductions, please keep in mind that taxpayers could also be audited by state taxing authorities. While I have given a quick overview of these areas I would certainly encourage anyone undergoing an audit to contact a tax professional.