

STATE OF WISCONSIN
TAX APPEALS COMMISSION

DUANE A. HENDRICKSON,

DOCKET NO. 06-I-81

Petitioner,

vs.

DECISION AND ORDER

WISCONSIN DEPARTMENT OF REVENUE,

Respondent.

DIANE E. NORMAN, ACTING CHAIRPERSON:

This matter came before the Commission for a telephone hearing on February 20, 2007. Petitioner, Duane A. Hendrickson ("petitioner"), appeared *pro se*. Respondent, Wisconsin Department of Revenue ("Department"), was represented by Attorney Sheree Robertson. The parties presented testimony and evidence at the hearing. Following the hearing, the Department filed a memorandum of law in this matter.

Having considered the entire record before it, the Commission finds, concludes, and orders as follows:

JURISDICTIONAL FACTS

1. On January 10, 2005, the Department sent a Notice of Amount Due to petitioner for an assessment ("the assessment") of income tax plus interest in the amount of \$6,563.39 for the years 2000, 2001 and 2002 ("the period under review"). Petitioner only disputes the portion of the assessment relating to deductions from his self-employment income.

2. By letter dated January 28, 2005, petitioner filed a request for redetermination of the assessment.

3. Under the date of January 18, 2006, the Department sent a Notice of Action to petitioner granting in part¹ and denying in part his petition for redetermination. This notice stated that the assessment of income tax plus interest for the period under review had been reduced to \$4,103.64.

4. On March 22, 2006, petitioner filed a timely petition for review with the Commission.

OTHER FACTS

5. Petitioner purchased a 60-acre piece of property in Balsam Lake, Wisconsin ("the property") in 1964 or 1965. He purchased the property as both a residence and income-producing property. Petitioner has a small residence on the property (32 ft. by 24 ft.) and two work/storage shops (24 ft. by 36 ft. and 18 ft by 30 ft.). On five acres of the property is an income-producing sand pit. Petitioner has plans to sell trees grown on the property, but had not sold any during the period under review.

6. The Department allowed petitioner to deduct 80% of the property's property taxes against petitioner's sand pit self-employment income for 2001 and 2002 even though the sand pit makes up approximately 12% of the property. The Department did not allow any deduction of property taxes for the year 2000 since petitioner failed to provide any documentation of the property taxes paid for that year. Petitioner did provide substantiation of the real estate taxes paid for the year 2000 after

¹ The Notice of Action stated that a portion of petitioner's claimed Schedule C business expenses were allowed.

the audit was completed in this matter.

7. In 2001, a storm caused damage to the property. Petitioner estimated the damage to the property at \$24,500. He testified that this figure represents the cost of clean-up for downed trees, replacement of shingles, repair of windows and damage to vehicles. Petitioner testified that the clean-up of the property has not yet been completed. Petitioner requested that a representative of the Department come to the property to see this storm damage, but the Department refused, citing the reasons that an inspection of the property would not determine the condition of the property before the storm as compared to after the storm and that too much time had elapsed since the storm in 2001.

8. Petitioner did not have insurance on the property and received no insurance proceeds as a result of the storm in 2001.

9. No appraisal of the property was completed before or after the storm in 2001. The only known valuation of the property is the assessed value for property tax purposes, which has increased in value since 2001.

10. Petitioner purchased a piece of equipment in 2001 known as a skid steer for approximately \$26,000. This equipment was deducted over a seven-year period of depreciation beginning in 2001.

11. During the audit of his 2001 income tax return, petitioner asked to change the method of deduction applied to the skid steer to Section 179 of the Internal Revenue Code ("I.R.C.") so that the entire cost of the skid steer could be deducted as an expense in that year. The Department would not allow this change in the depreciation method.

ISSUES

1. Did the Department err in its assessment by allowing petitioner to deduct 80% of his property taxes from his sand pit self-employment income for the years 2001 and 2002?
2. Did the Department err in its assessment by disallowing petitioner's claimed deduction for damages due to a storm in 2001?
3. Did the Department err in its assessment by not allowing petitioner to change the method of depreciation applied to the skid steer from a seven-year method to a one-time lump-sum method as allowed by I.R.C. § 179?

CONCLUSION OF LAW AND OPINION

Assessments made by the Department are presumed to be correct, and the burden is upon the petitioner to prove by clear and satisfactory evidence in what respects the Department erred in its determination. *Edwin J. Puissant, Jr. v. Dep't of Revenue*, Wis. Tax Rptr. (CCH) ¶ 202-401 (WTAC 1984); Wis. Stat. § 77.59(1). Tax exemptions, deductions, and privileges are matters of legislative grace and will be strictly construed against the taxpayer. *Fall River Canning Co. v. Dep't of Taxation*, 3 Wis. 2d 632, 637, 89 N.W.2d 203 (1958).

Deduction of Property Taxes

Internal Revenue Code § 162(a) provides for a deduction for "ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business. . . ." Additionally, I.R.C. § 212 provides for a deduction for "all the ordinary

and necessary expenses paid or incurred during the taxable year - (1) for the production or collection of income. . . ."

Petitioner's self-employment income is derived from a sand pit that makes up five acres of the property's 60 acres. Additional acreage is probably necessary to the business for a road to the sand pit and for storage/work shops. Since petitioner provided no specific evidence to show the exact portion of the property that is necessary to produce his self-employment income from the sand pit, the Department's allowance of 80% of the property's taxes for deduction in 2001 and 2002 is adequately supported by the record and also appears to be more than reasonable.

The reason cited by the Department as to why petitioner was not allowed to deduct any portion of the applicable property taxes for the year 2000 is that he failed to provide proof of payment of these taxes until after the audit was completed in this matter. Since he did provide substantiation documentation to the Department for this expense, 80% of his 2000 property taxes should also be allowed in this matter.

Therefore, petitioner has failed to show that the Department erred in allowing of the deduction of 80% of the property's property taxes for 2001 and 2002, but he shall be allowed to deduct 80% of the property's property taxes for the year 2000 as well.

Deduction for Storm Loss

Petitioner claimed a deduction of \$24,500 against his self-employment income from the sand pit on his property as reported on his 2001 income tax return. He testified that this is the amount he estimated would be needed to repair vehicles and

buildings and to clear downed trees on the property resulting from a storm that occurred in 2001.

The amount properly deducted from a taxpayer's income resulting from a casualty loss caused by a storm is the difference between the fair-market value before and after the storm. Treas. Reg. § 1.165-7(b) allows the deduction of the lesser of either the difference between the fair-market values before and after the casualty or the adjusted tax basis of the property.²

At the hearing before this Commission, the petitioner was unable to offer any substantial credible evidence as to his cost-basis and/or the fair-market value of the property and improvements thereon either before or after the 2001 storm. No appraisals had been completed to show a reduction in value of the property. According to petitioner, the only valuation of the property was the property tax assessment which had risen in value since the storm in 2001. Moreover, I.R.C. § 162 requires that “all ordinary and necessary expenses” of a business must be “paid or incurred during the taxable year.” Petitioner failed to provide any substantiation to show that he paid any expenses allocable to his estimate of \$24,500 paid in 2001 to repair machinery or buildings on the property that related to petitioner’s sand pit business. Petitioner admitted in his testimony that this was only an estimate and that much of the repairs had not yet taken place on the property. Since petitioner provided no substantiation to support his estimate of the cost of repairs to the property relating to the sand pit

² The Department also argues that there could be no casualty loss in this matter since the property was purchased for personal use. However, a portion of the property was used for business (an income producing sand pit) during the period under review.

business, petitioner has failed to show that the Department erred in not allowing any deduction for the storm damage in 2001.

Expense Depreciation

Petitioner claimed a depreciation deduction based on a seven-year period for a skid steer that was placed in service in 2001.³ Petitioner asked to change the method of depreciation to a one-time lump-sum depreciation method allowed by I.R.C. § 179.

The Department correctly decided that petitioner cannot change the method of depreciation used in the returns in this case at issue. According to Treas. Reg. § 1.179-5(a), he was required to elect the one-time Section 179 method in the year he filed his 2001 income tax return. Since he asked to change the method only after he had been audited in this matter, he could no longer change the depreciation method.

In sum, petitioner has failed to meet his burden of proving by clear and satisfactory evidence that the Department erred in the assessment, except that petitioner shall be allowed to deduct 80% of the property's property for the year 2000 since he provided substantiation for payment of the taxes required by the Department.

ORDER

1. Petitioner shall be allowed to deduct 80% of the property taxes he paid on the property for the year 2000.

³ Petitioner testified at the hearing that he may have depreciated another piece of equipment and not the skid steer in 2001 (a bulldozer placed in use in 1998), but he was not certain. In any event, petitioner had no documentation for a bulldozer. There was documentation to show that petitioner had placed a skid steer in operation in 2001 that had been purchased for \$26,000 and this amount had been used for a depreciation expense over a seven-year period.

2. In all other respects, the Department's action on petitioner's petition for redetermination is affirmed.

Dated at Madison, Wisconsin, this 22nd day of May, 2007.

WISCONSIN TAX APPEALS COMMISSION

Diane E. Norman, Acting Chairperson

David C. Swanson, Commissioner

ATTACHMENT: "NOTICE OF APPEAL INFORMATION"