LAW OFFICES

CROSBY GUENZEL LLP

FEDERAL TRUST BUILDING
134 SOUTH 13TH STREET, SUITE 400
LINCOLN, NEBRASKA 68508
TELEPHONE: (402) 434-7300
FACSIMILE: (402) 434-7303

WRITER'S E-MAIL: SGS@CROSBYLAWFIRM.COM
WRITER'S DIRECT DIAL NO. (402) 434-7324

WILLIAM D. KUESTER
STEVEN G. SEGLIN
ROCKY C. WEBER
DAVID A. JARECKE
WILLIAM R. KUTILEK
RICHARD L. RICE
THOMAS E. JEFFERS
MATHEW T. WATSON

THEODORE L. KESSNER (RETIRED)

ROBERT B. CROSBY (1911-2000)
ROBERT C. GUENZEL (1921-2007)

August 16, 2007

Jay Holmquist, General Manager
Nebraska Rural Electric Association
P.O. Box 82048
Lincoln, NE 68501

Re: Distinguishing Transportation Expenses and Travel Expenses for Purposes of Public Power District Board Members Mileage Reimbursement.

Dear Jay:

QUESTION

This opinion has been drafted as a follow-up to a memo previously prepared on August 2, 2007 entitled *Deductibility of Mileage Reimbursements for Public Power District Board Members* (the "Memo"). Research subsequent to the issuance of the Memo has modified its scope and further revealed additional questions that need to be addressed. The purpose of this opinion will be to expand upon the area not covered by the Memo and provide answers to additional questions which have subsequently arisen.

The focus of the Memo was primarily on the general law regarding business travel tax deductibility and how to determine what constitutes a taxpayer's principal place of business. Subsequent research has revealed that a distinction needs to be made when assessing business travel tax deductibility. This opinion distinguishes between two separate forms of business travel deductibility – travel expenses and transportation expenses. The Memo focused largely on travel expenses while this opinion focuses on the issue of transportation expenses. The significance of this distinction is that the breadth of deductibility for transportation expenses is much narrower than that for travel expenses under 26 USC § 162 ("section 162").

ANALYSIS

Travel expenses are unequivocally linked to the "away from home" requirement as discussed in Memo I. The "away from home" requirement necessitates a need for sleep or rest by the taxpayer during the business trip in order to be eligible for travel expense deductions under section 162. *Commissioner v. Bagley*, 374 F.2d 204, 205 (1st Cir. 1967). In the event the

"away from home" requirement is satisfied, the taxpayer may then deduct not only their transportation expenses, but also expenses for meals and lodging, provided they are related to an ordinary and necessary business expense. 519-2nd T.M., *Travel and Transportation Expenses – Deductions and Recordkeeping Requirements*, A-85 (2004). The import of the Memo is restricted to an assessment of the requirements related to travel expenses.

Differing from travel expenses, **transportation expenses** are deductible under section 162 without reversion to the "away from home" requirement. *Turner v. Commissioner*, 56 T.C. 27, 31 (1971). Additionally, unlike travel expenses, transportation expenses are primarily limited to the fuel expended to get from one location to another and the wear on the vehicle driven, and do not cover meals or other expenses incurred during the trip. "Deductible transportation costs are those costs, other than commuting costs, of transporting a person from one place to another in pursuit of a trade or business or an income-producing activity while that person is not in 'travel status,' i.e., not 'away from home' overnight or for a period requiring sleep or rest." 519-2nd T.M., *Travel and Transportation Expenses – Deductions and Recordkeeping Requirements*, A-85 (2004). When a board member travels to a board meeting, transportation expenses and not travel expenses are the proper form of tax deduction to be sought; provided, however, there is no sleep or rest required when traveling to the board meeting.

Whether a board member qualifies for a transportation expense deduction under section 162 is far from clear. Complicating this assessment is several factors, including but not limited to specific facts which may differ from one board member to another. From this point forward, this opinion will address several hypothetical factual situations which illustrate the varying circumstances that may exist from one board member to the next.

Example 1: A board member's sole employment is as a public power district board member. This board member travels to monthly board meetings by driving directly from his personal residence to the location of the board meeting.

Conclusion 1: The trip by car to and from the board member's personal residence and the location of the monthly board meeting is not deductible as it will be treated as a personal commute pursuant to 26 USC § 262 ("section 262"). It is a well settled rule that expenses associated with commuting by car from a residence to a business are non-deductible personal expenses under section 262. *Frederick v. United States*, 603 F.2d 1292, 1294 (8th Cir. 1979); *Kasun v. United States*, 671 F.2d 1059, 1061 (7th Cir. 1982).

Example 2: A board member maintains full-time employment that is separate from his position as a public power district board of director. The full-time job is not located at his personal residence. This board member travels to the monthly board meetings by driving directly from his separate place of employment to the location of the board meeting.

Conclusion 2: The trip between the board member's separate place of employment and the monthly board meeting is a deductible transportation expense pursuant to section 162(a). The trip from the monthly board meeting to the board member's personal residence is not deductible as it will be treated as a personal commute pursuant to section 262.

As set forth in *Curphey v. Commissioner*, 73 T.C. 766, 777 (1980), expenses incurred on trips between two places of business are deductible. (citing *Steinhort v. Commissioner*, 335 F.2d 496, 503-504 (5th Cir. 1964)). This rule allows for the transportation expenses between a board member's place of employment and the location of the board meeting to be deductible, but does not allow for a deduction when this board member travels from the location of the board meeting to his or her home.

The expenses incurred between the location of the board meeting and the board member's home would not be deductible as the trip would not be business related but instead related to personal motivations of the board member – to get home. *See Curphey*, 73 T.C. at 778. The reasoning behind the non-deductibility of the second leg of this trip is the same as that applied to a normal business commute by a taxpayer between his home and his place of business. The trip is not deductible because the taxpayer makes a personal choice in how close or far away from his business he elects to reside.

The extent of the deductibility of the trip between the board member's separate employment and the location of board meeting is strictly limited to the direct route between the two business locations. GCM 35201, *7 (1973). *Id.* Should the board member make personal stops or deviations when traveling between the two business locations, additional expenses incurred as a result of those deviations will not be deductible?

Example 3: A board member maintains full-time employment that is separate from his position as a public power district board of director. The full-time employment is not located at his personal residence. The board member travels to the monthly board meetings by driving directly from his personal residence to the location of the board meeting.

Conclusion 3: The trip to and from this board member's personal residence and the location of the board meeting is not deductible as it will be treated as a personal commute pursuant to section 262.

Even when a taxpayer works at two separate business locations on the same day, the direct route transportation costs between the two places of business will constitute nondeductible commuting expenses if the taxpayer returns to his or her residence prior to traveling to the second business location. GCM 35201, *7 (1973). It is clear that the IRS is insistent on the taxpayer traveling directly from one business to the other without stopping at his personal residence. An otherwise deductible trip is thereby transformed into a non-deductible trip if the taxpayer stops at his personal residence before traveling to the second business.

Example 4: A Board member maintains an office in his personal residence that is devoted solely to his or her business as a public power district board member. This board member travels to the location of the monthly board meeting by driving directly from his personal residence to the location of the board meeting.

Conclusion 4: The trip between the board member's personal residence and monthly board meeting will be deductible only if the nature of the use of the office at his or her residence qualifies as the principal place of business in relation to the work he performs for the public power district.

In order to qualify a board member's office as the principal place of business, certain requirements must be satisfied under 26 USC § 280A ("section 280A").

> Where a taxpayer's business is conducted in part in the taxpayer's residence and in part at another location, the following two primary factors are considered in determining whether the home office qualifies under section 280A(c)(1)(A) as the taxpayer's principal place of business: (1) The relative importance of the functions or activities performed at each business location, and (2) the amount of time spent at each location.

Harris v. Commissioner, T.C. Summary Opinion 2001-42, *24 (2001) (citing *Commissioner v. Soliman*, 506 U.S. 168, 175-177 (1993)). "'Principal place of business,' as that term is employed in section 280A(c)(1)(A), refers to the home as a specific situs in which a business is carried on." *Curphey*, 73 T.C. at 776. A taxpayer can have more than one principal place of business for purposes of section 280A(c)(1), if they engage in more than one trade or business. *Id.*

In addition to the requirements set forth above, section 280A requires that 1) the home office be used exclusively and regularly for administrative or management activities regarding the taxpayer's trade or business; and 2) that there be no other fixed location where the taxpayer conducts substantial administrative or management activities for their trade or business. To satisfy the exclusivity requirement, a person must use a specific area of their home solely for the trade or business they are participating in. This area can be a room or other separately identifiable space, so long as it is not conjunctively used for a non-trade or non-business related purpose (i.e. for personal or family purposes). Section 280A also contemplates the use of a building appurtenant to the board member's residence as a potential home office.

If a board member has satisfied the exclusivity requirement, he or she will then need to substantiate that the activity occurring within the space or office consisting of administrative or management activity. With respect to what constitutes an administrative activity, the IRS has identified the following illustrative but not exhaustive list of activities that will qualify: billing customers, clients or patients; keeping books and records; ordering supplies; setting up appointments; and forwarding orders or writing reports. IRS Publication 587 (p. 4).

With respect tot the fixed business location requirement, section 280A seems to prohibit the use of a secondary business location where substantial administrative or management activities are conducted; however, the IRS notes that occasionally conducting minimal administrative or management activities at a fixed location outside a person's home will not disqualify that person from characterizing their home as the principal place of business. IRS Publication 587 (p. 4). While some leniency may be afforded by the IRS, significance should

still be placed upon the substantive nature of the activities which occur at the secondary fixed location.

Ultimately, the determination as to whether a board member's home can qualify as their principal place of business will vary on a case by case basis, hinging upon whether a board member has devoted a specific area of his or her home to exclusively conducting business associated with the public power district. Even if a board member has fully appropriated the use of a portion of his home or established a separate office space solely for public power district business, it is still a question of fact as to whether the monthly business meetings conducted at a separate location would constitute more than minimal administrative or management activities; thereby precluding the designation of the board member's office as the only location where substantial administrative or management activities occur.

Given these considerations, qualifying a board member's office as the principal place of business with respect to the public power district will undoubtedly vary on a case by case basis. Furthermore, in connection with the factual scenario set forth in *Example 4*, a determination that substantial administrative and management activities occur at the monthly board meetings would likely preclude any board member from characterizing his office as the principal place of business with respect to his public power district activities.

Example 5: A Board member is a farmer and his personal residence also operates as his principal place of employment. This board member travels to the monthly board meetings by driving directly from his personal residence to the location of the board meeting.

Conclusion 5: It is clear that in certain situations, a taxpayer's home can also constitute their principal place of business for purposes of determining transportation expense deductibility. In the oft-cited tax case of *Curphey v. Commissioner*, 73 T.C. 766, 777-8 (1980), the Tax Court stated: "[w]e see no reason why the rule that local transportation expenses incurred in travel between one business location and another are deductible should not be equally applicable *where the taxpayer's principal place of business with respect to the activities involved is his residence.*" While cited with approval in many different forums, there is little consistency in the case law, private letter rulings, and general counsel memoranda regarding the breadth that should be afforded the tax principal espoused in the *Curphey* opinion.

With regard to farmers, there are two evident issues that must be addressed: 1) whether the farmer's residence also qualifies as a principal place of business with respect to the farming operations; and 2) whether a different rule applies when a taxpayer commutes between two business locations, neither of which are his residence, as opposed to when one of the business locations is also the taxpayer's residence, as with a farmer. It is noteworthy to mention that the IRS and tax courts have been less than clear and far from consistent when addressing this issue.

The statement in *Curphey*, 73. T.C. at 777-8, that transportation expenses are deducible "where the taxpayer's principal place of business with respect to the activities involved is his residence," leaves certain issues unresolved. It is particularly the phrase "with respect to the activities involved" that creates some ambiguity as to what transportation expenses are

deductible. The phrase seems to suggest that only transportation expenses which are associated with the particular business being conducted at the residence are deductible. The apparent meaning of this phrase would seem to run contrary to the aforementioned rule that transportation expenses between one place of business and a separate place of business are deductible. *See Example 2.*

This confusion is only further exacerbated by the Tax Court's opinion in *Freedman v. Commissioner*, 35 T.C. 1179 (1961). *Freedman* involved a personal injury action where the taxpayer was traveling between two separate jobs. In *Freedman*, the Court addressed the transportation issue as follows:

> Respondent has recognized that if an employee works for two separate employers in the same city on the same day, *both positions constitute part of the employee's trade or business (of being an employee)* and that local transportation expenses in getting from one place of employment to another constitute ordinary and necessary expenses in carrying on his combined trade or business, *even though the transportation expense is not incurred in discharging the duties of either job or in carrying on the business of either employer.*

35 T.C. at 1182 (emphasis added). While the *Freedman* opinion was issued before *Curphey* and did not involve the taxpayer's residence as a place of business, it does suggest there is no requirement that the transportation expenses incurred when traveling between two businesses be linked to either business.

Furthermore, and possibly even more significant, the *Freedman* court ruled that the employee's trade or business is "being an employee". This would seem to indicate that the "with respect to the activities involved" the requirement is satisfied when the taxpayer is traveling between two locations where he is an employee. If this is in fact the case, it would seem that a farmer traveling between one place of business where he is an employee, his farm, and a second place of business where he is an employee, the board meeting, would be incurring deductible transportation costs under section 162.

A potential weakness in this argument is that when the farmer leaves to or returns from the board meetings, he is not doing so in connection with his principal place of business but instead his home. This, in essence, suggests that when a person's residence is also their principal place of business, that location will wear two hats for tax purposes. It is then imperative to determine what role the residence is playing when the farmer travels to and from the board meeting – is he traveling to his principal place of business or his home? There has been little guidance by the courts and the IRS with respect to this issue.

In 1973, an IRS General Counsel Memoranda ("GCM"), GCM 35199, addressed a somewhat analogous situation to that experienced by board members who are also farmers.[1] The 1973 GCM focused on the issue of whether transportation costs incurred by a farmer in making daily round trips between his farm, where he both worked and resided, and a factory located in a nearby city where he was also employed, could be considered deductible business transportation expenses under section 162(a). There was no question that the farm was operated as a bona fide trade or business as the farmer worked on the farm daily, before and after his factory work, and also worked on the farm on days when he was not working at the factory.

In holding that the transportation costs were nondeductible commuting expenses, the GCM stated as follows: "[w]e do not think that otherwise nondeductible transportation costs incurred by a taxpayer in commuting from his residence to his place of work are transformed, in whole or in part, into deductible business transportation expenses by his performing work, whether substantial or insubstantial, at his residence." GCM 35199, *2.[2] The opinion of the IRS Chief Counsel in GCM 35199 is very much a conclusion without an explanation. The conclusion appears to fail to take into consideration two long-standing rules: 1) that a person's residence may also be their principal place of business; and 2) that travel between two places of business is deductible as a transportation expense under section 162.

Another hurdle for a farmer in characterizing his home as the principal place of business is whether an office maintained by a farmer would satisfy the section 280A requirements as set forth above. Since the business of farming is inherently a profession that requires its managers and employees to work outdoors and in the fields, it may be difficult to satisfy the exclusivity and administrative conditions of the home office requirements. The vast majority of opinions that have dealt with this issue have focused on the establishment of an office in the taxpayer's home with respect to professions such as doctors and salespersons – professions which inherently require the employees to conduct a substantial majority of their work in an indoor office environment. It may be difficult to establish that a separate room within the farmer's residence qualifies as an office where substantial administrative and management activities occur. Additionally, any room that has been allocated as an office must be used exclusively for business activities, which means dual uses of that room are prohibited. Given the unique nature of the farming profession, it is difficult to determine what the IRS would look towards to determine if the requirements of section 280A have been satisfied.

---

[1] "GCM's are legal memoranda from the Office of Chief Counsel to the Internal Revenue Service prepared in response to a formal request for legal advice from the Assistant Commissioner (Technical) . . . [and] are primarily prepared by attorneys in the Interpretative Division of the Office of Chief Counsel and usually addressed to the Office of the Assistant Commissioner (Technical) in connection with the review of proposed private letter rulings, proposed technical advice memoranda, and proposed revenue rulings of the IRS. *Taxation with Representation Fund v. IRS*, 485 F. Supp. 263, 265 (Dist. D.C. 1980).

[2] It may also be significant to note that it does not appear GCM 35199 was ever adopted as a Private Letter Ruling despite the Chief Counsel's recommendation that the memoranda be adopted. Furthermore, there is an instruction at the top of the GCM which states: "[t]his document is not to be relied upon or otherwise cited as precedent by taxpayers." Does the same hold true for tax assessors?

These are the primary considerations that must be taken into account when determining whether a board member who operates a farm operation may characterize that operation as a principal place of business in order to qualify for deductions under section 162A. As with *Example 4*, this assessment will likely vary in many instances on a case by case basis.

CONCLUSION

As it should be evident by a review of the foregoing examples, there are numerous issues that must be addressed in order to determine whether a board member can qualify for a deduction with respect to their transportation expenses to monthly board meetings. Since each board member's factual scenario undoubtedly varies in certain respects from other board members, a blanket conclusion regarding this matter is neither practical nor possible. Instead, each board member's situation will likely have to be addressed on a case by case basis with an individualized assessment undertaken to determine whether that particular board member may be eligible based upon one of the potential areas of deductibility for transportation expenses listed above.

Very truly yours,

CROSBY GUENZEL LLP

By

Steven G. Seglin
William R. Kutilek
Mathew T. Watson

SGS:rrk