

United States Tax Court

T.C. Memo. 2022-19

SHERWIN COMMUNITY PAINTERS INC.,
Petitioner

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent

ROBERT WARD, JR. AND SWANETTE TRIEM WARD,
Petitioners

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent

Docket Nos. 4113-19, 4647-19.

Filed March 9, 2022.

Leonard J. Gernstein, for petitioners.

Kaitlyn N. Christensen, Justin D. Scheid, and Kerrington A. Hall, for respondent.

MEMORANDUM OPINION

GOEKE, *Judge*: These consolidated cases have been submitted without trial pursuant to Rule 122.¹ Respondent determined a deficiency against Sherwin Community Painters, Inc. (Sherwin), of \$8,224 and an accuracy-related penalty under section 6662(a) for the

¹ Unless otherwise indicated, all statutory references are to the Internal Revenue Code, Title 26 U.S.C., in effect at all relevant times, all regulation references are to the Code of Federal Regulations, Title 26 (Treas. Reg.), in effect at all relevant times, and all Rule references are to the Tax Court Rules of Practice and Procedure.

Served 03/09/22

[*2] taxable year 2016. Respondent also determined a deficiency against Robert Ward, Jr., and Swanette Triem Ward of \$4,890 and an addition to the tax under section 6651(a)(1) for failure to timely file and an accuracy-related penalty under section 6662(a). After concessions, the issues for decision are: (1) whether Sherwin is entitled to certain business expense deductions; we hold it is to the extent set out below; and (2) whether Mrs. Ward received constructive dividends from Sherwin; we hold she did not. Petitioners have conceded the addition to tax and the penalties to the extent applicable.

Background

The following facts are derived from the Stipulations of Fact and Attachments. We overrule respondent's objections to three exhibits attached to the First Stipulation of Facts. Mr. and Mrs. Ward resided in Wisconsin when they timely filed their Petition. Sherwin, a C corporation, is solely owned by Mrs. Ward and had its principal place of business in Illinois when it timely filed its Petition. The Wards filed their 2016 joint tax return late on October 12, 2017.

Sherwin is a commercial painting contractor for commercial warehouses, residential complexes, and multipurpose highrise buildings. Both Mr. and Mrs. Ward work for the business. Sherwin receives customer referrals from property management companies. It claimed business expense deductions for office equipment, office supplies, gas, entertainment, and promotional materials. It also claimed a business expense deduction for the costs of a coding course at Northwestern University for Lucas Kocemba. The Wards met Mr. Kocemba in 2016 when he was dating their daughter. Mr. Kocemba expressed an interest in the course, and the Wards offered to pay the tuition if he was admitted. Before taking the course, he worked in the construction industry and had no previous coding experience. After completing the course in 2017, Mr. Kocemba used the skills that he had learned to update Sherwin's website over the course of several months and spent a considerable amount of time working on the website. Sherwin did not pay him for his work. Mr. Kocemba later married the Wards' daughter. He has performed additional computer-related work for Sherwin without compensation.

Discussion

Section 162(a) generally allows a deduction for the ordinary and necessary expenses paid during the taxable year in carrying on a trade

[*3] or business. The term “ordinary” means that the expense is normal, usual, or customary in the taxpayer’s trade or business. *Deputy v. du Pont*, 308 U.S. 488, 495 (1940). The term “necessary” means the expense is appropriate or helpful in carrying on the trade or business. *Heineman v. Commissioner*, 82 T.C. 538, 543 (1984). The expenses must proximately relate to the taxpayer’s trade or business. *Larrabee v. Commissioner*, 33 T.C. 838, 843 (1960); Treas. Reg. § 1.162-1(a). The determination of whether an expense satisfies the requirements for deduction is a question of fact. *Commissioner v. Heininger*, 320 U.S. 467, 475 (1943). A taxpayer is required to substantiate the expenses underlying a deduction by keeping and producing adequate records that enable the Commissioner to determine the correct tax liability, including the amounts paid; and to demonstrate that the deduction is allowable pursuant to some statutory provision. § 6001. A taxpayer is not entitled to deduct personal, living, or family expenses. § 262.

Respondent disallowed business expense deductions for Sherwin of \$26,500. After concessions, respondent challenges \$5,888.80 of the disallowed business expenses (excluding the tuition discussed below); on brief, Sherwin conceded \$2,056.54 of the disputed \$5,888.80. The unresolved expenses relate to office equipment and supplies and promotional materials. Petitioners have substantiated the amounts of the disputed expenses, and the remaining issue is the business purpose of the expenses. The office equipment expenses relate primarily to the purchase of iPads, iPhones, a speaker, and related expenses for service plans and an accessory. Petitioners assert that Sherwin’s employees use these items in the performance of their jobs. On the basis of the record, we accept petitioners’ assertion as to the business purpose and find that Sherwin has substantiated the amount and business purpose of each expense. We also accept petitioners’ proffered business purpose of office supplies and promotional items totaling \$387.08. Accordingly, Sherwin is entitled to deduct \$3,832.26 of the disputed expenses.

In addition to the deductions addressed above, Sherwin deducted the tuition that it paid for Mr. Kocemba’s coding course. Petitioners contend that Sherwin received website services in exchange for the tuition. While Mr. Kocemba has provided services to Sherwin free of charge that would have likely cost Sherwin more than the amount of the tuition, we nevertheless find that petitioners have not established that Sherwin is entitled to deduct the tuition. Mr. Kocemba was not an employee of Sherwin. The Wards did not have an agreement with Mr. Kocemba that he would perform any services in exchange for the tuition payment. Sherwin paid the tuition without any expectation of a return

[*4] and thus did not have a business purpose for the payment. The tuition was a personal expense, and Sherwin is not entitled to deduct it.

Respondent asserts that the Wards received a constructive dividend in the amount of the disallowed deductions. A constructive dividend arises when a corporation confers an economic benefit on a shareholder without an expectation of repayment where the corporation has current or accumulated earnings and profits. *Truesdell v. Commissioner*, 89 T.C. 1280, 1295 (1987). Constructive dividends are includible in the shareholder's gross income under section 61(a)(7).

In the notice of deficiency issued to the Wards, respondent recharacterized a shareholder loan made during 2016 of \$38,199 as a constructive dividend from Sherwin to Mrs. Ward. However, Sherwin records establish that the return reported that the loan was made from Mrs. Ward to Sherwin. Respondent refuses to concede his error and instead argues on brief that the disallowed business expense deductions should be treated as constructive dividends to Mrs. Ward. We reject this new position. There is no relationship between the disallowed expenses and the amount of the purported constructive dividends determined in the Wards' notice of deficiency. Sherwin's failure to substantiate the business purpose of the disallowed deductions does not render the amount a constructive dividend under the circumstances of these cases. There is no indication that the Wards received an economic benefit from the amount of disallowed expenses. Accordingly, we hold that the Wards did not receive any unreported dividends from Sherwin.

In reaching our holdings, we have considered all arguments made, and, to the extent not mentioned above, we conclude they are moot, irrelevant, or without merit.

To reflect the foregoing,

Decisions will be entered under Rule 155.