

# Step lively: When to count on the 'Cohan rule' for tax records

Let's be clear about this: There is no substitute for accurate record-keeping. The IRS insists on it. But in a pinch, you still might have an ace up your sleeve.

**Strategy:** Refer to the "Cohan rule." This court-created rule, named after a case involving the legendary Broadway hoofer, can bail you out of a tight jam if you don't have all the proper records.

The basic thrust is that you should be able to deduct some of the allowable expenses you've claimed, even without all the necessary records, if there's other credible evidence that those deductible expenses were actually incurred. A new case shows how the rule may be applied. (*Bauer, TC Memo 2012-156*)

**Key facts:** The taxpayer was in the business of helping people relocate by moving their furniture, appliances and other household goods. Typically, he was responsible for packing the items in boxes, loading them onto trucks or trailers, transporting them and unloading and unpacking the goods at the desired destination.

Generally, the taxpayer hired workers to help with the heavy lifting. He paid the workers \$10 to \$15 per hour, usually for a total of less than \$600. All payments were made in cash.

The taxpayer kept no records of the payments to workers or related expenses other than a logbook in which he recorded costs of relocation projects. He did not have the names or Social Security numbers of the workers nor did he issue any Forms 1099-MISC, *Miscellaneous Income*, reporting the amounts paid.

For the three tax years in question, the taxpayer reported gross receipts of close to \$200,000, plus contract labor expenses between \$42,000 and \$55,000 a year.

Despite the lack of records, the Tax Court gave the business owner a break. Because some expenses were clearly incurred, it used an industry report to calculate the allowable deductions for the labor the taxpayer had obviously hired.

The Tax Court arrived at a figure of close to \$12,000 for each of the three years. Of course, that was just a fraction of what the taxpayer had claimed on his returns, but it was still a whole lot better than nothing!

Once again, don't leave valuable tax deductions to chance. Reliance on the Cohan rule is a last resort rather than a recommended procedure.

**Tip:** Ironically, George M. Cohan claimed deductions for travel and entertainment (T&E), but the courts will no longer apply the rule named for him to T&E expenses.