

Boaters' Tales of Taxman Woe

by **Scott H. Novak**

It is the secret wish of every boater I know. We look at the expenses that our cherished passion demands and we start to fantasize. Not about great trips we might take, not about beautiful anchorages. No, many of us fantasize about the IRS adding a deduction line to our 1040 that would read "Boating Expenses." The directions for that line would say, "enter all boating expenses, including boat payments, dock charges, fuel costs, maintenance costs, insurance, cost of new toys purchased during the year, flip flops, ice, beer and fishing gear." If only it were so.

There are, of course, a couple of tax advantages that come along with most boats. The interest on a boat loan is deductible if the boat qualifies (sleeping quarters, cooking facilities, head). Sales tax can be deducted when you buy the boat. If you give your boat to a charity, you can likely take a deduction for the value of the boat. That way, the interest will remain deductible. But this is the run of the mill stuff that most boaters already know.

Ever since the first income tax, people have tried to be creative to make their tax bills as small as possible. Boaters are no exception. Some of them have run into trouble just by owning the boat and having an unrelated tax problem. Others have had far more creative situations that have worked or gone bust. So for my first contribution to Boating on the Hudson, I looked for tax trouble that some of our sea faring brethren have found themselves in.

The Captain With the Big Tax Bill

Sometimes it's simply more convenient to ignore the mail. Maybe you just don't want to deal with it. Like those pesky IRS or state tax notices. Ignore your teeth, they will go away. Ignore the tax man, he gets motivated. In some cases, a person who hasn't filed income taxes in several years may have moved and without notifying the tax people of the new address. He isn't ignoring the notices, the IRS is mailing them to his "last known address," as required under the law. The taxman doesn't know about the move – he is simply feeling ignored. And when he feels ignored, he likes to get your attention in dramatic fashion, really shake things up. Imagine showing up at the marina just in time to see your boat speeding out past the seawall, off to an IRS or New York State auction.

The internet is littered with boats being offered at auction by the IRS. One example as of this writing? A 1999 31' Sea Ray, "Five Hole," in Washington, NC. Twin Mercruisers, Raytheon electronics. 102 hours on the engines, 126 hours on the generator. Opening bid is \$24,000 (date of auction is 6/6). Maybe the owner should have named it "In the Hole." Along the road to auction are many opportunities to make things right with the tax folks and there are many strategies to get there if you cannot take care of the bill in one shot.

The Captain With the Bigger Tax Bill

Back in the late 1980s, a California businessman, Kent B. Rogers, convinced a federal judge that his back-tax bill for 1983 should be reduced to \$10.3 million from \$25 million. Apparently, that was a win. But Mr. Rogers, a real estate developer, failed to convince a different federal judge that IRS seizure of his 63-foot yacht Sundance was unreasonable. That left the yacht, his last remaining major asset, in the hands of the tax collectors. The IRS pointed out to the judge that Mr. Rogers had been convicted of bankruptcy fraud and had a pattern of hiding assets from creditors. The judge said that seizing the yacht was reasonable due in part to Rogers' "precarious financial status and propensities."

And how does someone come to owe more than \$10 million in income taxes? The IRS said most of the 1983 tax bill was based on money they had accused Rogers of embezzling from Bank of America in a \$95 million property fraud.

Captain Henry and His Floating Advertisement

For a business expense to be deductible, it has to be "ordinary" and "necessary." Mr. Henry, a New York accountant, flew a red, white and blue flag atop the mast of his boat with the numerals 1040 on it. Then he deducted his yacht expenses, contending that the boat with the flag brought him professional recognition and clients. The matter ended up in Tax Court. As it turned out, Captain Henry couldn't produce even one new client that was acquired through the flying "1040." The court ruled that the yacht wasn't a normal business expense for a tax pro, and so it wasn't "ordinary" or "necessary." The judge disallowed Mr. Henry's boat expenses of \$13,429, saying the boat was used for recreation, not to make a profit. (Henry v. CIR, 36 TC 879 (1961).)

Unusual advertising and public relations deductions have long been a bone of contention between taxpayers and the IRS. The IRS looks very carefully at and frequently challenges promotional expenses that appear to be personally motivated. The courts then have the job of settling the issue.

When the IRS or state tax folks come knocking, it may be a simple matter that can be handled through correspondence. For bigger issues, however, the stakes are high and you may want to consider getting professional help – either your accountant or a tax attorney.

Scott Novak is a fellow boater and an attorney who focuses on helping people and companies with tax problems, estate planning, trusts and other matters.

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