



United States Tax Court

Washington, DC 20217

CRAIG WALCOTT,

Petitioner

v.

COMMISSIONER OF INTERNAL
REVENUE,

Respondent

Docket No. 21820-22

ORDER

Pursuant to Rule 152(b), Tax Court Rules of Practice and Procedure, it is

ORDERED that the Clerk of the Court shall transmit herewith to petitioner and to respondent a copy of the pages of the transcript of the trial in the above case before Elizabeth A. Copeland at Anchorage, Alaska, containing her oral findings of fact and opinion rendered at the trial session at which the case was heard.

In accordance with the Oral Findings of Fact and Opinion, we will issue an Order requesting computations under Rule 155.

(Signed) Elizabeth A. Copeland
Judge

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IN THE UNITED STATES TAX COURT

In the Matter of:

CRAIG WALCOTT,

Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,

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Pages: 1 through 38

Place: Anchorage, Alaska

Date: June 3, 2026



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CRAIG WALCOTT,

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COMMISSIONER OF INTERNAL REVENUE,

Respondent.

Docket No. 21820-22

James M. Fitzgerald United States
Courthouse and Federal Building
222 West 7th Avenue
Room 229, Courtroom #4
Anchorage, Alaska 99513

June 3, 2026

The above-entitled matter came on for bench opinion,
pursuant to notice at 10:13 a.m.

BEFORE: HONORABLE ELIZABETH A. COPELAND
Judge

APPEARANCES:

For the Petitioner:

No Appearance

For the Respondent:

No Appearance

P R O C E E D I N G S

(10:13 a.m.)

THE CLERK: Recalling docket 21820-22, Craig
Walcott.

THE COURT: Thank you.

(Whereupon, a bench opinion was rendered.)

1 Bench Opinion by Judge Elizabeth A. Copeland
2 June 3, 2026
3 Craig Walcott v. Commissioner of Internal Revenue
4 Docket No. 21820-22

5 THE COURT: The Court has decided to render oral
6 findings of fact and opinion in this case, and the
7 following represents the Court's oral findings of fact and
8 opinion. The oral findings of fact and opinion shall not
9 be relied upon as precedent in any other case. The oral
10 findings of fact and opinion are made pursuant to the
11 authority granted by section 7459(b) of the Internal
12 Revenue Code and Tax Court Rule 152. Unless otherwise
13 noted, section references in this opinion are to the
14 Internal Revenue Code, Title 26 U.S.C. (I.R.C.), in effect
15 at all relevant times, regulation references are to the
16 Code of Federal Regulations, Title 26 (Treas. Reg.), in
17 effect at all relevant times, and rule references are to
18 the Tax Court Rules of Practice and Procedure. All
19 monetary amounts are stated in U.S. dollars and, at times,
20 rounded to the nearest dollar.

21 Petitioner, Craig Walcott, disputes two Notices
22 of Deficiency (collectively, "Notices"), both of which
23 were issued by the Internal Revenue Service (IRS) on June
24 29, 2022. One of the Notices was for the 2013 tax year,
25 and one was for both the 2012 and 2014 tax years. We will

1 refer to the 2012, 2013, and 2014 tax years collectively
2 as "years at issue."

3 For tax year 2012, the Commissioner of Internal
4 Revenue (Commissioner) determined a deficiency of \$78,887
5 and asserted a failure-to-file addition to tax under
6 section 6651(a)(1) of \$19,722 and an accuracy-related
7 penalty under section 6662(a) of \$15,777. For tax year
8 2013, the Commissioner determined a deficiency of \$48,533
9 and asserted a failure-to-file addition to tax of \$12,133.
10 For tax year 2014, the Commissioner determined a
11 deficiency of \$46,661 and asserted a failure-to-file
12 addition to tax of ^{\$11,665}~~\$11,655~~ and an accuracy-related penalty *Ear*
13 of \$9,332.

14 We must address all issues in the Notices;
15 however, we note that the adjustments to other taxes are
16 purely computational as is the deduction for one-half of
17 self-employment taxes. Such computational adjustments
18 will not be separately addressed.

19 On the evidence before us, and using the burden-
20 of-proof principles explained below, the Court finds the
21 following facts:

22 FINDINGS OF FACT

23 In the years at issue, Mr. Walcott operated a
24 business selling nutritional supplements. Mr. Walcott was
25 also the direct owner or manager of multiple properties in

1 Colorado from which he received rental income. Finally,
2 he started a skin care business in 2014.

3 On or around July 20, 2014, a tax return was
4 filed for tax year 2013 for Mr. Walcott. The IRS has
5 determined that this return was the result of identity
6 theft and was not filed by Mr. Walcott. This return
7 claimed that Mr. Walcott had \$67,401 of W-2 wages from a
8 pet hospital in Minnesota, had a tax liability of \$6,385,
9 but had \$13,189 of withheld taxes, and was thus entitled
10 to a refund of \$6,804 (i.e. \$13,189-\$6,385). The tax
11 liability from that return was assessed; but upon the
12 finding of identity theft, such assessment was removed.

13 On February 26, 2019, Mr. Walcott filed Forms
14 1040, U.S. Individual Income Tax Return, for tax years
15 2012, 2013, and 2014. Each of the returns included a
16 Schedule C, Profit or Loss from Business, for Mr.
17 Walcott's supplement business. For 2014, Mr. Walcott
18 attached an additional Schedule C for what the return
19 described as his "[s]kin care" business, operated under
20 the name of "GAIRC LLC." Only the 2013 return included
21 Schedule D, Capital Gains and Losses. All returns for the
22 years at issue included Schedule E, Supplemental Income
23 and Loss, for Mr. Walcott's rental income.

24 For the years at issue, all returns were
25 prepared by Laurie's Bookkeeping & Tax Service. The 2012

1 return reported \$30,822 of taxable income and showed a
2 total tax liability of \$13,980. The 2013 return reported
3 \$76,468 of taxable income and showed a total tax liability
4 of ~~\$29,387~~ ^{\$29,397}. The 2014 return reported \$103,079 of taxable ✓
5 income and showed a total tax liability of \$38,695.

6 On June 29th, 2022, Commissioner issued the
7 aforementioned two Notices of Deficiency to Mr. Walcott.
8 For the 2012 year, in an attached Form 886-A, Explanation
9 of Items, the Commissioner explained that he made the
10 following adjustments. The Commissioner increased Mr.
11 Walcott's income by \$18,530, due to Charles Schwab
12 reporting that amount of original issue discount (OID)
13 interest. The Commissioner attributed to Mr. Walcott an
14 additional short-term capital loss of \$2,840. On Mr.
15 Walcott's Schedule C, the Commissioner disallowed all
16 \$18,133 of Mr. Walcott's claimed cost of goods sold
17 (COGS), and all \$72,985 of Mr. Walcott's claimed business
18 expenses (Mr. Walcott had claimed expenses for the
19 categories of advertising, car and truck expenses,
20 contract labor, legal and professional services, office
21 expenses, supplies, travel, deductible meals and
22 entertainment, and other expenses which were comprised of
23 bank fees, postage, a donation, and bad debts). The
24 Commissioner stated that it was disallowing the COGS and
25 business expenses because Mr. Walcott had not shown that

1 the expenses were both paid and ordinary and necessary to
2 his business. On Mr. Walcott's Schedule E, the
3 Commissioner increased rents received to \$44,043 to
4 account for \$27,095 reported on a Form 1099 by Global
5 Realty USA Inc., \$3,214 from a bank deposit by Proficient
6 Property Management Services, and \$13,734 of rental
7 deposits not reported on Form 1099, resulting in increased
8 income of \$15,397 for rental activities. The Commissioner
9 disallowed \$6,748 of rental expenses that Mr. Walcott
10 claimed on his Schedule E, alleging a lack of
11 substantiation. The Commissioner adjusted the number of
12 Mr. Walcott's dependents from one to zero, on the grounds
13 that Mr. Walcott had not established that he was entitled
14 to the exemption for the dependent. Finally, the
15 Commissioner disallowed all of the \$74,792 cost basis Mr.
16 Walcott had claimed for a rental house that he had sold
17 and reported on Form 4797, Sales of Business Property, as
18 the Commissioner stated that Mr. Walcott had not
19 established this cost basis.

20 For the tax year 2013, because of the identity
21 theft adjustments, the tax liability from Mr. Walcott's
22 late-filed return was not assessed, and the Commissioner's
23 Notice of Deficiency, with attached Form 4549-A, Report of
24 Income Tax Examination Changes, and the Form 886-A,
25 incorporates the income from that late-filed return rather

1 than adjusting it. Consistent with tax year 2012, no
2 expenses are allowed and his filing status is married
3 filing separately. In contrast, Mr. Walcott's
4 aforementioned late-filed 2013 return claimed numerous
5 items of income and expense.

6 According to the Commissioner's Form 886-A for
7 tax year 2013, Mr. Walcott's correct tax attributes are as
8 follows. He had income of \$1,951 from original issue
9 discount taxable interest, a figure reported on a 1099-OID
10 by Charles Schwab. He had Schedule C gross receipts of
11 \$150,845, the sum of figures reported on Forms 1099-MISC
12 by Doctor's Signature Sales, DBA Life Force International,
13 and by AL Global Corporation, DBA Youngevity. He had
14 Schedule C COGS of \$7,547. He had no Schedule C expenses.
15 He had a long-term capital gain of \$4,284, a figure which
16 the Commissioner obtained from a Charles Schwab statement.
17 He had no other long-term capital gain or losses. He had
18 Schedule E rents received of \$18,150. He had no Schedule
19 E expenses. These figures, when combined with a self-
20 employment deduction and the standard deduction, resulted
21 in a taxable income of \$153,751, and an initial tax of
22 \$38,124. When combined with self-employment tax, net
23 investment income tax, and an additional Medicare tax, the
24 result was a total tax of \$48,533 (Mr. Walcott reported
25 \$29,397). See I.R.C. § 6211(a) (explaining the

1 computation of a deficiency).

2 On Mr. Walcott's actual return for 2013, he
3 reported Schedule C gross receipts of \$147,501, COGS of
4 \$9,085, and Schedule C expenses of \$34,122, resulting in a
5 Schedule C net profit of \$104,294. On Schedule D, Capital
6 Gains and Losses, he also reported various long-term
7 capital gains and losses which resulted in a net long-term
8 capital gain of \$4,284 (the same as allowed in the Notice
9 of Deficiency). He had Schedule E rents received of
10 \$18,150, and Schedule E total expenses of \$52,511. He
11 reported two dependents. The total tax shown on his
12 return was \$29,397.

13 For tax year 2014, the Commissioner made the
14 following adjustments. He disallowed \$4,254 of Mr.
15 Walcott's reported \$11,782 for COGS for Schedule C1 (his
16 nutritional supplement business). He allowed some of Mr.
17 Walcott's Schedule C1 expenses but disallowed the
18 following categories: travel, car and truck expenses,
19 utilities, office expenses, meals and entertainment, legal
20 and professional services, repairs and maintenance, and
21 other expenses. He disallowed the entirety of Mr.
22 Walcott's Schedule C2 expenses (his skin care business) in
23 the categories of advertising, car and truck expenses,
24 contract labor, legal and professional services, office
25 expenses, rent or lease of other business property,

1 repairs and maintenance, travel, deductible meals and
2 entertainment, utilities, and other expenses.

3 As to the Schedule C1 expenses, the Notice of
4 Deficiency's attached Form 886-A, Explanation of Items,
5 contained several discrepancies. It stated that the
6 amount of Mr. Walcott's Schedule C1 expenses for
7 advertising, contract labor, and supplies, both "Per
8 return," and "Per exam," were \$0. In the attached Form
9 4549-B, Report of Income Tax Examination Changes, no
10 adjustments were made to Schedule C1 advertising, contract
11 labor, or supplies for tax year 2014. Mr. Walcott's
12 Schedule C1 reported \$14,147 in advertising, \$2,400 in
13 contract labor, and \$1,200 in supplies expenses.

14 The Notice of Deficiency also had some
15 discrepancies regarding the Schedule C1 other expenses.
16 Mr. Walcott's return listed three types of other expenses:
17 \$386 of bank fees, \$3,801 of postage, and \$928 of
18 "Charities." This sums to \$5,115. But on Mr. Walcott's
19 return, it appears that for the "Total", first one string
20 of numerals were typed, and then, perhaps to correct a
21 mistake, another string of numerals were typed over the
22 first string. The exact numerals that made up each of the
23 two strings are not clear. Mr. Walcott then needed to use
24 the amount of other expenses in order to calculate his
25 "Total expenses before business use of home." In doing

1 so, he seems to have assumed that the other expenses
2 figure was \$13,266 rather than \$5,115. The Commissioner
3 himself misread the figure as \$15,255, and disallowed all
4 of it, thus using the incorrect figure of \$15,255 in
5 calculating adjustments to income, which in effect would
6 have resulted in an increase to income and inaccurate
7 deficiency.

8 The Commissioner also disallowed all Schedule E
9 rental expenses, disallowed the deduction for self-
10 employed health insurance, adjusted the number of Mr.
11 Walcott's dependents from one to zero, and changed Mr.
12 Walcott's filing status from head of household to married
13 filing separately.

14 Mr. Walcott resided in Alaska when he timely
15 filed his Petition in this case.

16 OPINION

17 I. *Burden of Proof*

18 As a general matter, the Commissioner's
19 determinations in a Notice of Deficiency are presumed
20 correct, and the taxpayer bears the burden of proving an
21 error. Rule 142(a); *Welch v. Helvering*, 290 U.S. 111, 115
22 (1933). Determinations of unreported income must be
23 supported by "a minimal evidentiary foundation" before the
24 presumption of correctness applies. *Feathers v.*
25 *Commissioner*, T.C. Memo. 2024-88, at *11, n.16 (citing

1 *Weimerskirch v. Commissioner*, 596 F.2d 358, 361 (9th Cir.
2 1979)). However, the IRS may not rely solely on a third-
3 party report of income, such as Form W-2 or 1099-R, if the
4 taxpayer raises a reasonable doubt concerning the accuracy
5 of the report and has fully cooperated with the Secretary.
6 See I.R.C. § 6201(d).

7 For tax year 2012, the IRS alleges the following
8 unreported income items: \$18,530 of original issue
9 discount interest, and an additional \$15,397 of rents
10 received arising from three sources -- \$27,095 from Global
11 Realty USA Inc., \$3,214.37 from Proficient Property
12 Management Services, and \$13,733.54 from unnamed sources,
13 a total of \$44,043 rather than the \$28,646 reported by Mr.
14 Walcott (\$44,043-\$28,646=\$15,397). Mr. Walcott's receipt
15 of the original issue discount interest is no longer at
16 issue, because in an Order issued May 22, 2026, we deemed
17 this amount admitted. With respect to the rents received,
18 the Notice of Deficiency states that the Global Realty
19 amount is substantiated by a Form 1099, the Proficient
20 Property Management Service amount is substantiated by
21 "bank deposits," and the unnamed sources amount is
22 substantiated by "rental deposits not reported on Form
23 1099." None of this substantiation, however, appears to
24 be in the record; and the Commissioner did not provide any
25 such substantiation at trial. Therefore, the Commissioner

1 has not provided a minimal evidentiary foundation, and
2 thus the presumption of correctness does not apply to the
3 unreported rents received for 2012.

4 For tax year 2013, the IRS alleges the following
5 unreported income items: \$1,951 of original issue
6 discount interest, and an additional \$3,344 (i.e. \$150,845
7 reported on Forms 1099 less the amount claimed on Mr.
8 Walcott's return (\$147,501)) of Schedule C gross receipts
9 from a combination of Doctor's Signature Sales, DBA Life
10 Force International, and AL Global Corp., DBA Youngevity.
11 Mr. Walcott's receipt of these items is no longer at
12 issue, as in the aforementioned Order issued May 22, 2026,
13 we deemed this admitted. (We note that we actually deemed
14 admitted one dollar more of Schedule C gross receipts than
15 was alleged in the Notice of Deficiency, likely due to
16 rounding.)

17 For tax year 2014, the IRS alleged no unreported
18 income.

19 *II. Unreported Income*

20 As we have just discussed, the Commissioner did
21 not put forth any evidence showing that Mr. Walcott
22 received the remaining unreported income at issue -- the
23 alleged additional rents received for tax year 2012.
24 Therefore, as the Notice of Deficiency receives no
25 presumption of correctness for this item, we do not

1 sustain the Commissioner's determination of this one
2 unreported income item.

3 *III. Mr. Walcott's Frivolous Arguments Concerning Income*

4 In this case, Mr. Walcott contested the
5 Commissioner's determinations in part by offering
6 unsupported arguments that his earnings are not taxable.

7 As we previously explained in our Order issued
8 May 11, 2026 (Index No. 65), we have held that "it is
9 usually *not* expedient to discuss and refute in detail the
10 frivolous arguments that some litigants attempt to press
11 in the Tax Court," and "litigants who press such arguments
12 are not entitled to and should not expect to receive
13 opinions rebutting their frivolous arguments." *Wnuck v.*
14 *Commissioner*, 136 T.C. 498, 513 n.14 (2011).

15 Our reasons for this include the following:
16 "The number of potential frivolous anti-tax arguments is
17 unlimited." *Id.* at 501. "A frivolous anti-tax argument
18 may be unimportant even to its proponent." *Id.* at 502.
19 "Many frivolous arguments have already been answered."
20 *Id.* at 503. ^{The} ~~A~~ litigant who presses the frivolous anti- *SAC*
21 tax arguments often fails to hear its refutation." *Id.* at
22 504. "Many frivolous anti-tax arguments are patently so."
23 *Id.* at 505. "Addressing frivolous anti-tax arguments
24 wastes resources." *Id.* at 510. "The time taken to
25 address frivolous anti-tax arguments delays the assessment

1 of tax." *Id.* at 511. "Addressing frivolous anti-tax
2 arguments risks dignifying them." *Id.* at 512.

3 For these reasons, "Courts confronting frivolous
4 arguments against constitutionality, validity, and
5 applicability, and mandatory character of income tax often
6 aptly quote *Crain v. Commissioner*, 737 F.2d 1417 (5th Cir.
7 1984), which stated, 'We perceive no need to refute these
8 arguments with somber reasoning and copious citation of
9 precedent.'" *Wnuck*, 136 T.C. at 499.

10 Turning to the case at hand, Mr. Walcott alleges
11 that the Supreme Court's holding in *Moore v. United*
12 *States*, 602 U.S. 572 (2024), supports his position that
13 the revenue he received from sales, interest, and renting
14 real estate is not taxable income. Mr. Walcott's argument
15 seems to be that (Premise 1) *Collins v. United States*, 920
16 F.2d 619 (10th Cir. 1990) held that the income tax is a
17 direct tax. (Premise 2) *Moore* invalidated *Collins* and
18 instead held that the income tax is an indirect excise
19 tax. (Premise 3) Indirect excise taxes only apply to
20 people engaging in specific activities or transactions.
21 (Premise 4) Mr. Walcott did not engage in any such
22 specific activities or transactions. Therefore, (his
23 Conclusion) the income tax does not apply to him.

24 Apart from the citation to *Moore*, which held
25 that indirect taxes on income from whatever source derived

1 are clearly constitutional, this is a frivolous argument
2 that we have repeatedly rejected. See, e.g., *Smith v.*
3 *Commissioner*, T.C. Memo. 2019-111, at *10 ("Petitioners'
4 final argument is that the income tax is an excise tax and
5 [but for one exception] they did not engage in activities
6 subject to excise tax during the years in question.
7 Numerous courts, including this Court, have rejected that
8 argument as meritless, and we see no need to entertain it
9 any further.")

10 Mr. Walcott's citation to *Moore* does not improve
11 this frivolous argument. He does not point to any
12 particular citation in *Moore* or quote any language from
13 it. *Moore* indeed states that "indirect taxes are the
14 familiar federal taxes imposed on activities and
15 transactions. That category of taxes includes duties,
16 imposts, and excise taxes, as well as income taxes,"
17 *Moore*, 602 U.S. at 582-83, and "[t]axes on income --
18 including taxes on income from property -- are indirect
19 taxes." *Id.* at 583. And Mr. Walcott is indeed correct
20 that, if the Supreme Court's holding in *Moore* contradicts
21 the ^{Tenth} ~~Ninth~~ Circuit's holding in *Collins*, then *Moore* gave
22 controls. See, e.g., *Hutto v. Davis*, 454 U.S. 370, 375.
23 ("[A] precedent of [the Supreme] Court must be followed by
24 the lower federal courts...."). But *Moore* nowhere
25 suggests that the income tax fails to apply to Mr.

1 Walcott's activities and transactions -- his selling of
2 nutritional supplements and skin care, his ~~running~~^{renting} out of ^{SAC}
3 property. The actual holding in *Moore* is that a certain
4 tax not related to Mr. Walcott (the Mandatory Repatriation
5 Tax) "falls squarely within Congress's constitutionality
6 authority to tax," *id.* at 598 (emphasis added), and the
7 Supreme Court expressly stated that "we emphasize that our
8 holding today is narrow." *Id.* at 598. It is not
9 reasonable to read *Moore* and conclude that the Supreme
10 Court in its "narrow" holding upholding the
11 constitutionality of a particular tax, somehow at the same
12 time invalidated large swaths of income tax.

13 Therefore, Mr. Walcott's arguments are not
14 sound, and his earnings are taxable.

15 IV. *Business Expenses: General Principles*

16 Deductions are a matter of legislative grace,
17 and taxpayers bear the burden of proving the entitlement
18 to any deduction claimed. *INDOPCO, Inc. v. Commissioner*,
19 503 U.S. 79, 84 (1992). A taxpayer must show that he has
20 met all requirements for each deduction and must keep
21 books or records that substantiate expenses underlying it.
22 I.R.C. § 6001; *Roberts v. Commissioner*, 62 T.C. 834, 836
23 (1974). Failure to keep and present such records counts
24 heavily against a taxpayer's attempted proof. *Rogers v.*
25 *Commissioner*, T.C. Memo. 2014-141, at *17.

1 Section 162(a) allows a deduction for "ordinary
2 and necessary expenses paid or incurred during the taxable
3 year in carrying on any trade or business." Whether an
4 expenditure is "ordinary and necessary" is generally a
5 question of fact. *Commissioner v. Heininger*, 320 U.S.
6 467, 475 (1943). To be "ordinary", the expense must be a
7 common or frequent occurrence for the taxpayer's type of
8 business. *Deputy v. Du Pont*, 308 U.S. 488, 495 (1940).
9 An expenditure is "necessary" if it is "directly connected
10 with" and "appropriate and helpful" to the taxpayer's
11 business. *Welch v. Helvering*, 290 U.S. 111, 113 (1933);
12 Treas. Reg § 1.162-1(a). No deduction is allowed for
13 "personal, living, or family expenses." I.R.C. § 262(a).

14 If a taxpayer proves that deductible expenses
15 were incurred but cannot establish the precise amounts,
16 the Court in appropriate circumstances may estimate the
17 deductions allowable. See *Cohan v. Commissioner*, 39 F.2d
18 540, 543-44 (2d Cir. 1930). However, there must be
19 sufficient evidence in the record to supply a rational
20 basis for such an estimate. *Vanicek v. Commissioner*, 85
21 T.C. 731, 742-43 (1985); see *Lerch v. Commissioner*, 877
22 F.2d 624, 627-29 (7th Cir. 1989) (refusing to apply the
23 *Cohan* rule where the taxpayer failed to present evidence
24 to support a reasonable estimate), *aff'g* T.C. Memo. 1987-
25 295.

1 Section 274(d) sets forth heightened
2 substantiation requirements (and overrides the Cohan rule)
3 for certain types of expenses. As in effect during the
4 years at issue, section 274(d) made these strict
5 requirements applicable for "any traveling expense
6 (including meals and lodging while away from home)," "any
7 item with respect to an activity which is of a type
8 generally considered to constitute entertainment,
9 amusement, or recreation, or with respect to a facility
10 used in connection with such an activity," "any expense
11 for gifts," and "any listed property (as defined in
12 section 280F(d)(4))." "Listed property" is defined to
13 include "any passenger automobile." I.R.C. §
14 280F(d)(4)(A)(i).

15 With respect to these items, section 274(d)
16 provides that no deduction shall be allowed "unless the
17 taxpayer substantiates by adequate records or by
18 sufficient evidence corroborating the taxpayer's own
19 statements" the following facts:

20 (A) the amount of such expense or other item,
21 (B) the time and place of the travel [or]
22 entertainment...or the date and description of
23 the gift, (C) the business purpose of the
24 expense or other item, and (D) the business
25 relationship to the taxpayer ^{of} ~~or~~ persons

lac

1 entertained...or receiving the gift.

2 See Temp. Treas. Reg. § 1.274-5T(c).

3 For expenses governed by section 274(d),
4 "[w]ritten evidence has considerably more probative value
5 than oral evidence," and "the probative value of written
6 evidence is greater the closer in time it relates to the
7 expenditure." Temp. Treas. Reg. § 1.274-5T(c)(1).

8 Substantiation by "adequate records" generally requires
9 the taxpayer to "maintain an account book, diary, log,
10 statement of expense, trip sheets, or similar record" to
11 document the expenditure. *Id.*, subpara. (2). An actual
12 contemporaneous log is not strictly required, but records
13 made at or near the time of the expenditure have greater
14 probative value than records created subsequently. *Id.*
15 subparas. (1) and (2).

16 Lastly, we discuss the standard for COGS. COGS
17 is subtracted from gross receipts to determine gross
18 income. Treas. Reg. § 1.61-3(a). Technically speaking,
19 COGS is not a "deduction." See *Metra Chem Corp. v.*
20 *Commissioner*, 88 T.C. 654, 661 (1987). It is the cost of
21 acquiring inventory, through either purchase or
22 production. *Patients Mut. Assistance Collective Corp. v.*
23 *Commissioner*, 151 T.C. 176, 205 (2018), *aff'd*, 995 F.3d
24 671 (9th Cir. 2021). Taxpayers must keep records to
25 enable the IRS to verify any amount claimed as COGS. See

1 I.R.C. § 6001; *Kalk v. Commissioner*, T.C. Memo. 2024-82,
2 at *9; Treas. Reg. § 1.6001-1(a).

3 *V. Schedule C1 Business Expenses (Direct Sales)*

4 We start with COGS. During the years at issue,
5 Mr. Walcott operated a legitimate business selling
6 nutritional supplements. He testified that he incurred
7 COGS in purchasing these supplements to sell to his
8 customers, and he supported this testimony with credit
9 card account statements. Particularly as to the 2013 tax
10 year, those statements show multiple purchases from the
11 nutritional supplement businesses of Youngevity and Life
12 Force closely approximating the amounts reported on Mr.
13 Walcott's late-filed returns. As well, Mr. Walcott's
14 testimony was credible on this point, and we hold that Mr.
15 Walcott is entitled to the entirety of his claimed amounts
16 of COGS for the years at issue for his direct sale
17 business.

18 We now turn to Mr. Walcott's Schedule C1 expense
19 deductions.

20 First, we address the strict substantiation
21 expenses. Mr. Walcott claimed Schedule C1 deductions for
22 the categories of car and truck expenses, deductible meals
23 and entertainment, and travel. These expenses are subject
24 to the strict substantiation requirements of section
25 274(d). Mr. Walcott provided account statements showing

1 that certain purchases were made, but the account
2 statements did not establish that these purchases had a
3 business purpose. Nor did they show the identity of any
4 persons who were entertained and their business
5 relationship to Mr. Walcott. The record contained no
6 account books, diaries, mileage logs, or trip sheets that
7 documented the business purpose of these expenses.
8 Therefore, they do not meet the strict substantiation
9 requirements of section 274(d), and we sustain the
10 Commissioner's disallowance of these expenses for all the
11 years at issue.

12 Next, we address the remaining categories of
13 Schedule C1 expenses.

14 Advertising expenses were substantiated by Mr.
15 Walcott's testimony and his account statements with
16 numerous charges from businesses such as Facebook and
17 Google. For 2013, however, these charges summed to only
18 \$1,955 of Mr. Walcott's claimed \$8,672. He is therefore
19 entitled to only \$1,955 in advertising expenses for that
20 year. For 2012, the expenses do not appear on his
21 statements, but he credibly testified that he incurred
22 them, and he claimed the amount of \$2,670, consistent with
23 the charges for 2013. We therefore hold that Mr. Walcott
24 is entitled to \$2,670 in advertising expenses for 2012.
25 As for 2014, the Commissioner did not contest Mr.

1 Walcott's claimed advertising expenses.

2 Contract labor was not adequately substantiated.
3 Mr. Walcott did not provide evidence showing that the
4 claimed amounts were paid for business purposes. We
5 accordingly sustain the disallowance of these deductions
6 for lack of substantiation.

7 Legal and professional services were a mixed
8 bag. For 2012, Mr. Walcott on his return claimed \$11,782,
9 but at trial he pointed to a Form 1099-MISC which he
10 filled out for a \$15,000 payment, and he credibly
11 testified that this payment was for legal and professional
12 services. We accordingly hold that he is entitled to
13 deduct \$15,000 for legal and professional services for
14 2012. For 2013, he claimed only \$3,959, but the only
15 written documentation he provided to substantiate this
16 claim was an invoice for \$1,675. We believe Mr. Walcott
17 concerning the business purpose of this invoice, but we
18 are not convinced there were any other legal and
19 professional service payments, and so we hold that Mr.
20 Walcott is entitled to deduct only \$1,675 in this category
21 in 2013. For 2014, Mr. Walcott did not provide evidence
22 that the claimed amounts were paid in the required tax
23 years for business purposes. We accordingly sustain the
24 disallowance of these deductions in 2014 for lack of
25 substantiation.

1 Office expenses were not completely
2 substantiated. Mr. Walcott claimed larger amounts than
3 one would expect from a nutritional supplement seller, and
4 his account statements did not establish that the
5 purchases were for business, as opposed to personal,
6 purposes. We believe that Mr. Walcott incurred some
7 office expenses, but since we cannot establish what
8 percentage of his claimed expenses were for business
9 purposes, we apply the *Cohan* rule and allow him 25% of his
10 claimed expenses, or \$1,540, \$584, and \$1,386 for tax
11 years 2012, 2013, and 2014, respectively.

12 Rent or lease of other business property was not
13 adequately substantiated. Mr. Walcott only claimed this
14 category for 2014, and in the amount of \$300 for that
15 year. He did not provide substantiation demonstrating
16 that such amounts were paid for business purposes. We
17 accordingly sustain the disallowance of this deduction for
18 lack of substantiation.

19 Repairs and maintenance were only deducted in
20 2014. Mr. Walcott did not provide substantiation
21 demonstrating that such amount was spent for business
22 purposes. We accordingly sustain the disallowance of this
23 deduction for lack of substantiation.

24 Supplies were not adequately substantiated;
25 however, the Commissioner only challenged this expense for

1 2012 and 2013. As with office expenses, Mr. Walcott
2 claimed larger amounts than one would expect from a seller
3 of nutritional supplements, and his account statements did
4 not establish that the purchases were for business, as
5 opposed to personal, purposes. We accordingly sustain the
6 disallowance of these deductions for lack of
7 substantiation as to the two years noted.

8 Utilities were partially substantiated, but Mr.
9 Walcott did not break out the amounts allocable to his
10 real estate business or his personal usage. Looking at
11 his account statements, in 2013 we see that \$1,338 of
12 charges, whereas he reported \$2,073; and in 2014 we see
13 \$1,267, whereas he reported \$600. We therefore hold that
14 he is entitled to \$1,338 and \$1,267 for those years,
15 respectively. In 2012, his statements do not reflect
16 utility expenses, but we believe Mr. Walcott's testimony
17 that he incurred such, and so we apply the *Cohan* rule and
18 allow 50% of his claimed expenses, or \$1,650.

19 The category of Other Expenses was another mixed
20 bag. Mr. Walcott claimed the following expenses in this
21 category: for 2012 -- bank fees, postage, a donation, and
22 bad debts; for 2013 -- bank fees, postage, and web design;
23 for 2014 -- bank fees, postage, and charities. For bank
24 fees, postage, and shipping, these are expected expenses
25 of a direct-to-consumer sales business, and Mr. Walcott

1 adequately substantiated them for all years at issue. For
2 web design, we are uncertain of the exact amounts of
3 payments with a business purpose and so we will apply the
4 *Cohan* rule and allow Mr. Walcott 50% of these claimed
5 deductions. For the rest -- a donation, bad debts, and
6 charities -- Mr. Walcott did not provide adequate
7 substantiation of what these charges were and how they
8 were ordinary and necessary for his nutritional
9 supplements business. We accordingly sustain the
10 disallowance of these expenses due to lack of
11 substantiation for all years at issue.

12 VI. *Schedule C2 Business Expenses (Skin Care)*

13 Solely for the 2014 tax year Mr. Walcott also
14 included a second Schedule C for a skin care business.
15 There was limited discussion at trial regarding this
16 business, and no separate substantiation was provided.

17 Mr. Walcott reported \$8,775 of gross receipts,
18 \$2,988 of Cost of Goods Sold and \$30,373 of total
19 expenses, including advertising, car & truck, contract
20 labor, legal and professional, office, rent, repairs,
21 travel, meals and entertainment, utilities, and other
22 (bank fees, shipping, amortization, business property,
23 startup costs, and postage). We have no basis for
24 estimating or upholding either the Cost of Goods Sold or
25 the business expenses deducted, and they will be

1 disallowed accordingly.

2 VII. *Schedule E Real Estate Expenses*

3 With respect to his activities renting out and
4 managing real estate, Mr. Walcott claimed Schedule E
5 expenses in the following categories: auto and travel,
6 cleaning and maintenance, insurance, management fees,
7 mortgage interest, other interest, repairs, taxes,
8 utilities, depreciation expense or depletion, and other
9 expenses. In the Notices of Deficiency, the Commissioner
10 disallowed all of Mr. Walcott's Schedule E expenses.

11 Mr. Walcott claimed large amounts of expenses
12 relative to his real estate income. In every tax year,
13 and for every rental property, his total expenses exceeded
14 his rents received. He deducted only a portion of the
15 losses due to passive activity loss limitations. See
16 I.R.C. § 469 (disallowing certain passive activity
17 losses).

18 The insurance expenses were adequately
19 substantiated by Mr. Walcott. The taxes were not
20 substantiated enough to enable us to identify the exact
21 amount, and so we will apply the *Cohan* rule and allow Mr.
22 Walcott 50% of his claimed expenses in this category. As
23 regards depreciation expenses, Mr. Walcott did not provide
24 evidence of the cost basis in the properties which would
25 allow us to determine the correct depreciation amount, and

1 so we sustain its disallowance by the Commissioner. As
2 regards all the other categories -- auto and travel,
3 cleaning and maintenance, management fees, mortgage
4 interest, other interest, repairs, utilities, and other
5 expenses -- other than some discussion of a repair to
6 kitchen tiles in his Auburn property rental, and some
7 discussion of a \$20,779 mortgage redemption payment on the
8 Palmer Park rental, both incurred in 2012, Mr. Walcott did
9 not point the Court to evidence supporting the claimed
10 amounts deducted on his real estate business. We note
11 that for each year at issue, Mr. Walcott deducted the
12 exact same amount in repairs for each of his rental
13 properties (\$1,540 for each property in 2012, \$2,337 for
14 each in 2013, and \$11,001 for each in 2014). This is
15 implausible. As for the mortgage redemption payment, Mr.
16 Walcott was confused as to whether he owned or managed the
17 related property; and other than self-prepared
18 spreadsheets, he provided no evidence of that payment.
19 Therefore, we sustain the Commissioner's disallowance of
20 other categories of real estate expense deductions.

21 *VIII. Cost Basis on Form 4797, Sales of Business Property*

22 Mr. Walcott credibly testified that he bought a
23 mobile home, rented it out, had problems with the tenants,
24 and eventually decided to sell the mobile home at a loss.
25 He claimed a gross sales price of \$39,520, depreciation

1 allowable since acquisition of \$6,838, a cost or other
2 basis of \$74,792, and thus a loss of \$25,999 (i.e., the
3 gross sales price plus the depreciation allowable, less
4 the basis). The Commissioner determined that Mr. Walcott
5 had not substantiated his cost basis in the mobile home,
6 and so he had a gain of \$46,358, (i.e. the gross sales
7 price plus the depreciation allowable). We believe Mr.
8 Walcott's testimony that he paid some amount for the
9 mobile home, but he has no written substantiation, and we
10 are unsure of the exact amount. Since we may apply the
11 *Cohan* rule to estimate a taxpayer's basis in an asset,
12 see, e.g., *Wheeler v. Commissioner*, T.C. Memo. 2014-204,
13 at *7, we do so and estimate that his basis was \$46,358,
14 enough to cover the sales price and depreciation, but no
15 more. Therefore, Mr. Walcott has neither gain nor loss
16 from this sale of business property.

17 IX. *Filing Status for 2014*

18 On his return for 2014, Mr. Walcott chose a head
19 of household filing status. This filing status is
20 generally available only for individuals who are not
21 married at the close of their taxable year, I.R.C. §
22 2(b)(1), although there is an exception for certain
23 married individuals living apart, I.R.C. §§ 2(c); 7703(b).
24 At trial, Mr. Walcott testified that he was married at the
25 close of 2014, and he gave no indication that he and his

1 wife were living apart. We therefore sustain the
2 Commissioner's determination that Mr. Walcott's filing
3 status was married filing separately, the filing status he
4 chose for other tax years at issue.

5 X. *Dependents*

6 On his returns, Mr. Walcott claimed one
7 dependent, two dependents, and one dependent for tax years
8 2012, 2013, and 2014, respectively. The Commissioner
9 determined that he had not substantiated his entitlement
10 to any of these dependents, and thus for each year was
11 entitled to none.

12 Section 151(c) allows as a deduction an
13 exemption for each dependent of a taxpayer in computing
14 taxable income. Section 152(a) provides that a dependent
15 means a "qualifying child" or a "qualifying relative." To
16 be a qualifying child, an individual must not provide more
17 than one-half of his or her own support, I.R.C. §
18 152(c)(1). To be a qualifying relative, an individual
19 must have over one-half of his or her support provided by
20 the taxpayer. I.R.C. § 152(d)(1)(C).

21 Mr. Walcott testified at trial that the
22 dependents he claimed were his children, and that they
23 were in college during the years at issue. He submitted
24 no evidence showing that they failed to provide over one-
25 half their own support in the years at issue, and so he

1 did not establish that they were qualifying children. He
2 also submitted no evidence that he himself provided over
3 one-half of their support during the years at issue, and
4 so he did not establish that they were qualifying
5 relatives. We therefore sustain the Commissioner's
6 determination that Mr. Walcott is not entitled to
7 dependents for the years at issue, due to a lack of
8 substantiation.

9 *XI. Accuracy-Related Penalty*

10 With respect to the accuracy-related penalties,
11 section 6662(a) provides that a taxpayer may be liable for
12 a penalty of 20% of the portion of an underpayment of tax
13 required to be reported on a return that is attributable
14 to, among other things, negligence or disregard of the
15 rules or regulations or a substantial understatement of
16 income tax. See I.R.C. § 6662(b)(1) and (2). Under
17 section 7491(c), the Commissioner bears the burden of
18 production with respect to penalties and must provide
19 evidence that a penalty is appropriate. *Higbee v.*
20 *Commissioner*, 116 T.C. 438, 446 (2001).

21 For those section 6662 penalties that require
22 managerial approval, the Commissioner must establish
23 compliance with section 6751(b). *Walquist v.*
24 *Commissioner*, 152 T.C. 61, 68 (2019). In the United
25 States Court of Appeals for the Ninth Circuit, the circuit

1 court to which this case is presumably appealable, see
2 I.R.C. § 7482(b), written supervisory approval must be
3 obtained "before the assessment of the penalty or, if
4 earlier, before the relevant supervisor loses discretion
5 whether to approve the penalty assessment." *Laidlaw's*
6 *Harley Davidson Sales, Inc. v. Commissioner*, 29 F.4th
7 1066, 1074 (9th Cir. 2022), *rev'g and remanding* 154 T.C.
8 68 (2020). For tax year 2013, the Commissioner asserted
9 no section 6662(a) penalty. For tax years 2012 and 2014,
10 the Commissioner has introduced evidence showing that the
11 examining agent's immediate supervisor approved the
12 assertion of the penalty on June 21, 2022. Mr. Walcott's
13 Notices of Deficiency were issued on June 29, 2022. The
14 Commissioner has therefore demonstrated compliance with
15 section 6751(b).

16 Application of the accuracy-related penalty may
17 be avoided with respect to any portion of an underpayment
18 for which a taxpayer shows that he had reasonable cause
19 and acted in good faith. I.R.C. § 6664(c)(1); *Higbee*, 116
20 T.C. at 446-47. The determination of whether the taxpayer
21 had reasonable cause and acted in good faith depends upon
22 the facts and circumstances of a particular case. Treas.
23 Reg. § 1.6664-4(b)(1). We consider among other factors,
24 the experience, education, and sophistication of the
25 taxpayer; however, the principal consideration is the

1 extent of the taxpayer's efforts to assess the proper tax
2 liability. *Id.*; see also *Higbee*, 116 T.C. at 448. Taking
3 into consideration the taxpayer's experience, education,
4 and sophistication, an honest misunderstanding of fact or
5 law may indicate reasonable cause and good faith. *Higbee*,
6 116 T.C. at 449 (citing *Remy v. Commissioner*, T.C. Memo.
7 1997-72).

8 Mr. Walcott has not argued nor demonstrated that
9 he had reasonable cause for his understatement.
10 Accordingly, we sustain the accuracy-related penalty under
11 section 6662(a) for tax years 2012 and 2014.

12 XII. Section 6651(a)(1) Addition to Tax

13 Section 6651(a)(1) imposes an addition to tax
14 for failure to timely file a federal income tax return
15 unless the taxpayer shows that the failure was due to
16 reasonable cause and not due to neglect. See *Higbee*, 116
17 T.C. at 446-47. The addition applies at a rate equal to 5
18 percent of the amount required to be shown as tax on the
19 return for each month in which the failure to pay
20 persists, up to a maximum of 25 percent. Sections 6011
21 and 6012 require every individual who has gross income
22 above the exemption amount to file an income tax return.
23 The Commissioner established both that Mr. Walcott had
24 gross income above that threshold and that he did not
25 timely file a return. Mr. Walcott has not argued that he

1 had reasonable cause for his failure to timely file his
2 return. Accordingly, we sustain the addition to tax for
3 failure to timely file under section 6651(a)(1) for all
4 tax years at issue.

5 *XIII. Section 6673 Sanctions*

6 This Court now considers whether to impose
7 sanctions under section 6673(a)(1). Section 6673(a)(1)
8 authorizes the Court to impose a penalty of up to \$25,000
9 for frivolous arguments or whenever it appears to the
10 Court that proceedings before us "have been instituted or
11 maintained by the taxpayer primarily for delay." In an
12 Order issued May 11, 2026, this Court warned Mr. Walcott
13 about the section 6673 penalties.

14 The positions Mr. Walcott advanced at trial were
15 frivolous, and this Court is justified in sanctioning him.
16 However, because Mr. Walcott focused at trial on non-
17 frivolous arguments that he is entitled to certain
18 deductions, and because this is Mr. Walcott's first trial
19 before this Court, we decline to impose the section 6673
20 penalty at this time. We warn him to refrain from
21 advancing frivolous arguments in any future filings he may
22 make in this Court, as they may subject him to penalties.
23 Additionally, as the Court already stated on the record,
24 we warn Mr. Walcott that if he advances frivolous
25 arguments on appeal in a United States Circuit Court of

1 Appeals, that Court may impose a penalty.

2 XIV. Rules 33 and 202 Sanctions

3 Mr. Walcott requested that we sanction the
4 Commissioner's counsel under Rules 33 and 202. Mr.
5 Walcott's grounds are as follows. He argues that the
6 Commissioner's labeling of Mr. Walcott's positions as
7 frivolous is itself frivolous. He also argues that it was
8 improper for the Commissioner to request 6673 penalties
9 for Mr. Walcott, and to refuse to respond to Mr. Walcott's
10 questions in discovery which were predicated upon
11 frivolous legal assertions.

12 Rule 33 provides that counsel must sign each
13 pleading and certify that "to the best of the signer's
14 knowledge, information, and belief, formed after
15 reasonable inquiry, it is well grounded in fact and is
16 warranted by existing law or by a nonfrivolous
17 argument...and that it is not presented for any improper
18 purpose...." Rule 50(a) states that motions must be
19 similarly signed.

20 Rule 202 provides that "a member of the Bar of
21 this Court may be disciplined by this Court as a result
22 of" conduct which "violates the letter and spirit of the
23 Model Rules of Professional Conduct of the American Bar
24 Association, the Rules of the Court, or orders or other
25 instructions of the Court; or [a]ny other conduct

1 unbecoming of a member." Discipline may consist of any
2 sanction "that the Court may deem appropriate."

3 Mr. Walcott's positions which the Commissioner
4 labeled frivolous were indeed frivolous, and thus it was
5 not improper for the Commissioner to request section 6673
6 penalties for Mr. Walcott or to refuse to answer certain
7 questions predicated upon those positions. Therefore, we
8 will not impose sanctions against the Commissioner's
9 counsel under Rules 33 and 202.

10 *XV. Conclusion*

11 For the reasons described above, we conclude
12 that Mr. Walcott (1) had no additional rents received in
13 2012, (2) is entitled, for all tax years at issue, to his
14 COGS as well as certain Schedule C expense deductions for
15 his direct sales business limited as outlined previously,
16 and his Schedule E expenses in the amounts previously
17 stated, (3) has neither gain nor loss from the 2012 sale
18 of his mobile home, (4) has a filing status of married
19 filing separately for tax year 2014, (5) is not entitled
20 to claim exemptions for dependents for the years at issue,
21 and (6) is liable for the accuracy-related penalties and
22 failure-to-file additions to tax. We refrain from
23 sanctioning Mr. Walcott under section 6673, and we decline
24 to sanction the Commissioner's counsel under Rules 33 and
25 202.

1 To reflect the foregoing, a decision will be
2 entered under Rule 155.

3 This concludes the Court's oral findings of fact
4 and opinion in this case.

5 (Whereupon, the above-entitled matter was
6 concluded at 11:19 a.m.)

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1 CERTIFICATE OF TRANSCRIBER AND PROOFREADER

2 CASE NAME: Craig Walcott v. Commissioner

3 DOCKET NO.: 21820-22

4 We, the undersigned, do hereby certify that the
5 foregoing pages, numbers 1 through 38 inclusive, are the
6 true, accurate and complete transcript prepared from the
7 verbal recording made by electronic recording by Bruce
8 Carlson on June 3, 2026 before the United States Tax Court
9 at its session in Anchorage, AK, in accordance with the
10 applicable provisions of the current verbatim reporting
11 contract of the Court and have verified the accuracy of
12 the transcript by comparing the typewritten transcript
13 against the verbal recording.

14

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16

17

18 Hana Copperman, CET-487

6/29/26

19 Transcriber

Date

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23

24 Traci Fine, CDLT-169

7/1/26

25 Proofreader

Date

