JACKIE L & STEPHANIE SPARKS 1909 SANDFORT RD PHENIX CITY, AL 36869,	§ §	STATE OF ALABAMA DEPARTMENT OF REVENUE ADMINISTRATIVE LAW DIVISION
Taxpayers,	§	DOCKET NO. INC. 04-888
v.	§	
STATE OF ALABAMA DEPARTMENT OF REVENUE.	§	

FINAL ORDER

The Revenue Department assessed Jackie L. and Stephanie Sparks (together "Taxpayers") for 2001 and 2002 Alabama income tax. The Taxpayers appealed to the Administrative Law Division pursuant to Code of Ala. 1975, §40-2A-7(b)(5)a. A hearing was conducted on March 31, 2005. The Taxpayers attended the hearing. Assistant Counsel Margaret McNeill represented the Department.

Jackie Sparks (individually "Taxpayer") raced automobiles on dirt tracks during the years in issue. The Taxpayers deducted the racing expenses on their 2001 and 2002 Alabama returns. The issue is whether those expenses can be deducted as ordinary and necessary business expenses. That issue turns on whether the Taxpayer conducted his racing activities for the primary purpose of making a profit.

The Taxpayer worked full time for CV Holdings in Auburn, Alabama during the years in issue. His wife worked for AFLAC in Phenix City, Alabama. Together they received wage income of approximately $70,000 in each of the subject years.

The Taxpayer testified that his father and uncle raced cars on dirt tracks when he was young. He bought a car when he turned 21 and started racing himself. He is now in his early 30's, and has owned 4 different race cars. He performs all of the maintenance and repairs on the vehicles.

The Taxpayer enters approximately 35 to 40 races a year. He testified that he cannot afford to race without working. Consequently, he arranges his racing schedule around his work schedule. Two or three of the Taxpayer's friends usually travel with him to the races and help him change tires, maintain the vehicle, etc.

When asked at the March 30 hearing why he raced, the Taxpayer responded – "For the fun of it, you know, playing around (with) it. I'd like to quit my job and go racing for a living. I mean, but I can't just quit (my job) and go do that. I'd – I'd like to." (T. 9.)

The Taxpayers reported net losses from the racing activities of between $12,000 and $13,000 on their 2001 and 2002 Alabama returns. When asked if he would continue racing if he continued to lose that amount of money, the Taxpayer responded – "Probably. It's like bass fishing. You've got to buy the boat, you know." (T. 14.)

Code of Ala. 1975, §40-18-15(a)(1) allows a deduction for all ordinary and necessary expenses incurred in a trade or business. Section 40-18-15(a)(5) also allows a deduction for non-business losses incurred in a transaction entered into for profit. Both statutes are modeled after their federal counterparts, 26 U.S.C. §§162 and 212, respectively. Consequently, federal case law interpreting the federal statutes should be followed in interpreting the similar Alabama statutes. *Best v. Dept. of Revenue*, 417 So.2d 197 (Ala. Civ. App. 1981).

The general test for whether a taxpayer is engaged in a "trade or business," and thus entitled to deduct all ordinary and necessary business expenses, is whether the taxpayer's primary purpose in engaging in the activity is to make a profit. *Zell v. Commissioner of Revenue*, 763 F.2d 1139 (10th Cir. 1985). To be deductible, the activity must be engaged in "with a good faith expectation of making a profit." *Zell*, 763

F.2d at 1142. Whether the taxpayer had an intent to make a profit is a question of fact that must be determined from all the circumstances. *Patterson v. U.S.*, 459 F.2d 487 (1972).

In *State of Alabama v. Dawson*, Inc. 85-130 (Admin. Law Div. 11/19/85), the issue was whether the taxpayer's drag racing activities constituted a trade or business. The taxpayer in *Dawson* incurred net losses during the years in issue, 1982 and 1983, and also failed to keep business records of his racing activities in those years. Based thereon, the Administrative Law Division held that the activity was not entered into for profit, and consequently that the taxpayer's racing expenses were not deductible.

The Court of Civil Appeals reversed. See, *State, Dept. of Revenue v. Dawson*, 504 So.2d 312 (Ala. Civ. App. 1986). The Court explained that racing was the taxpayer's only moneymaking activity during the subject years, and that he spent most of his time and energy on his racing activities. The Court further explained that the taxpayer incurred losses in the subject years primarily because he had just begun racing, and thus had extraordinary "start-up" expenses in those years. Also, the taxpayer's expenses were less in 1984, and he made a small profit in that year. The Court opined that the taxpayer failed to maintain adequate records because he had little formal education and no training in maintaining business records. The Court thus concluded that the taxpayer's racing activities were entered into for profit.

The facts in this case can be distinguished from the facts in *Dawson*. First, the taxpayer's primary activity and only moneymaking endeavor in *Dawson* was drag racing. In this case, the Taxpayer's primary income-producing activity was his job with CV Holdings. He testified that he could not continue racing without keeping his day job.

Second, the losses in *Dawson* were incurred primarily because the taxpayer had extraordinary start-up expenses in the subject years concerning his drag racing activities. The Taxpayer in this case has been racing for over ten years. Consequently, his losses in 2001 and 2002 cannot be explained as "start-up" expenses.

The Taxpayer testified that he would like to quit his job and race full-time. That hope does not appear to be realistic because there is no evidence the Taxpayer has ever made an annual profit from racing. His gross income from racing was only $1,050 in 2001 and $1,135 in 2002. As indicated, the Taxpayer also testified that he raced because he enjoyed it, and that he would probably continue racing even if he continued to lose money.

I appreciate the honest, sincere testimony of the Taxpayer and his wife. Under the circumstances, however, the facts establish that the Taxpayer did not conduct his racing activities with the reasonable expectation of making a profit. Dirt track racing is the Taxpayer's lifelong hobby, not his business. Consequently, the racing-related expenses were properly denied by the Department.

The final assessments are affirmed. Judgment is entered against the Taxpayers for 2001 tax and interest of $269.52, and 2002 tax and interest of $680.53. Additional interest is also due from the date of entry of the final assessments, September 20, 2004.

This Final Order may be appealed to circuit court within 30 days from the date of this Order pursuant to Code of Ala. 1975, §40-2A-9(g).

Entered May 19, 2005.

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BILL THOMPSON
Chief Administrative Law Judge