COMMONWEALTH OF MASSACHUSETTS

APPELLATE TAX BOARD

SARAH P. THAYER **v.** **COMMISSIONER OF REVENUE**

Docket No. C308533

Promulgated:
December 17, 2014

This is an appeal filed under the formal procedure pursuant to G.L. c. 58A, § 7 and G.L. c. 62C, § 39 from the refusal of the Commissioner of Revenue ("Commissioner" or "appellee"), to abate income taxes assessed against Sarah P. Thayer ("Dr. Thayer" or "appellant") for tax years 2006, 2007, and 2008 ("tax years at issue").

Chairman Hammond heard this appeal and was joined by Commissioners Scharaffa, Rose, Chmielinski and Good in a decision for the appellee.

These findings of fact and report are made pursuant to requests by both parties under G.L. c. 58A, § 13 and 831 CMR 1.32.

Stephen M. Politi, Esq. for the appellant.

Kevin M. Daly, Esq. and *Keri Angus*, Esq. for the appellee.

FINDINGS OF FACT AND REPORT

On the basis of the testimony and exhibits offered into evidence at the hearing of this appeal, the Appellate Tax Board ("Board") made the following findings of fact.

I. INTRODUCTION AND JURISDICTIONAL BACKGROUND

The appellant, a resident of Massachusetts, is a cancer surgeon and assistant professor of surgery at Massachusetts General Hospital ("MGH"). She also serves as Director of the Pancreatic Biology Research Laboratory at MGH, where she managed a large staff and a budget of several million dollars. The appellant owned horses which were boarded in the Commonwealth. Over the tax years at issue, the number of horses owned by Dr. Thayer increased from one to three. Dr. Thayer claimed the expenses associated with the care of the animals, which ranged from $114,368 to $190,326 per year during the tax years at issue, as deductible business expenses for income tax purposes. The appellant argued that these expenses were incurred as part of a trade or business that she conducted to purchase and train horses for lease or sale, a business which she referred to in tax filings for the tax years at issue as "Simply the Best Baroch."

The appellant timely filed income tax returns for each of the tax years at issue. Pursuant to an audit of the appellant's tax returns for the 2006, 2007, and 2008 tax years, the

Commissioner issued the appellant a Notice of Assessment on November 24, 2009, assessing additional income tax of $6,049 for the 2006 tax year, $9,966 for the 2007 tax year, and $8,704 for the tax year 2008, plus statutory interest of $2,574.30, resulting in a total assessment of $27,293.30.

On January 4, 2010, the appellant filed an application for abatement for the tax years at issue. On May 7, 2010, the Commissioner issued a Notice of Abatement Determination denying the appellant's application. On July 6, 2010, the appellant timely filed this appeal with the Board. On the basis of these facts, the Board found and ruled that it had jurisdiction over this appeal.

The Board heard testimony over two days of hearings. The appellant presented her case-in-chief through: her own testimony; the testimony of Lynn O'Connell, the owner and operator of Wadsworth Farm in Danvers, Massachusetts where Dr. Thayer's horses were boarded during the tax years at issue; and the testimony of Nora Petralta, the Department of Revenue's auditor who conducted the audit of the appellant's tax filings. Ms. O'Connell has owned and operated Wadsworth Farms since 1996 and has extensive experience with buying, selling, training, and riding horses. The appellant also introduced exhibits including expense records, calendar logs, medical records for her horses, horse show records, profit projections for each horse, a written

valuation of one of her horses done by Ms. O'Connell and a corresponding unexecuted contract for her to represent the appellant in a potential sale of that horse, and the appellant's Internal Revenue Service audit file for the tax years at issue.

II. APPELLANT'S HORSE-RELATED ACTIVITIES

The appellant is a prize-winning dressage horse rider who testified that she has trained with highly acclaimed teachers, including Olympic level riders. Dressage horse riding is a sport where horses and their riders are judged on their abilities to execute a series of skills. The appellant testified that she could not "remember a time when [she] didn't have an education as an equine person." She began riding horses in her youth, eventually owning her own horse in high school that she subsequently took with her to college and medical school. After graduating from medical school, Dr. Thayer went on to earn a Ph.D. in New York. While a student in New York, she purchased a horse named "Baroch." As she continued her studies, she testified that she taught riding lessons for money and allowed others to rent Baroch for lessons or training, even as she continued to ride and train. In 1998, the appellant began a surgery residency at MGH in Boston and boarded Baroch at Wadsworth Farm, the horse barn owned and operated by Lynn O'Connell. Baroch subsequently became ill and died prior to the tax years at issue.

1. "Simply the Best Baroch" Business

In February 2002, the appellant bought a young, unbroken[1] stallion named "Simply the Best" ("Simply") for $37,500. Dr. Thayer testified that she purchased the animal with the intent of training it as a dressage horse and re-selling it at a profit at a later date. She testified that while she had owned horses in the past, Simply was the first horse she purchased with the intent of entering into the business of selling horses. The appellant has filed a Schedule C reporting losses from equine activity since 1998, a business which she referred to as "Baroch" on her tax filings. She claimed that the prior activity with Baroch was a distinct business activity, as he was a hunter-jumper horse instead of a dressage horse. However, the Board found that there was no evidence to support that there was any meaningful distinction between "Baroch" and "Simply the Best Baroch," and found that the purchase of Simply was merely a continuation of the equine activities which she had claimed on her Schedule C since 1998.

The appellant testified that there is a "very standard model" in the equine business, involving two occasions that present "real opportunities to make profit" selling a horse – either immediately after breaking and initial training, where

[1] "Breaking" a horse refers to the training process to allow a horse to accept a rider.

value is largely based on the horse's raw potential, or upon the horse's successfully reaching the "Prix St. George," a level of international competition. The appellant testified that there are many levels of competition for dressage horses through which a horse must pass as it develops. The appellant testified that the rise through the ranks contains several "tollgates," or major watershed advancements. For example, the Prix St. George is considered such a tollgate, as it is the first of the international competition levels. Both the appellant and Ms. O'Connell testified that a dressage horse's value is largely tied to its ability to meet these tollgates throughout its development.

Throughout the tax years at issue, the appellant was employed by MGH. She testified that she worked extremely long hours at MGH, including her duties as a surgeon, her duties at the laboratory, and her duties as a professor, in addition to times when she was "on-call." Nevertheless, the appellant testified that she spent an average of 25 to 29 hours a week riding and training her horses at Wadsworth Farm or otherwise involved in their care. Dr. Thayer testified that she spent any vacation time she had from her practice working with her horses.

i. Simply the Best

The appellant's purchase of Simply was made on the recommendation of Wadsworth Farm's then head trainer, Roel

Theunissen, who served as the agent for the sale. At the time, Simply was located in the Netherlands, where he received strong evaluations from European judges; the appellant testified that the judges ranked him among the forty best stallions in the Netherlands. Simply remained in the Netherlands for several months while he was broken and he was brought to Wadsworth Farm in 2002. When Simply arrived at Wadsworth Farm, the appellant engaged Mr. Theunissen to train him to perform as a dressage horse.

The appellant testified that an "unexplained lameness" was first noticed in Simply's front leg around 2004. Dr. Thayer consulted with several veterinarians regarding the problem, including a number of specialists, but no satisfactory diagnosis was reached as to the nature of the lameness. Unexplained lameness would have been a significant barrier to a potential sale of the animal. The appellant testified that she sent Simply to Georgia in 2005, where Mr. Theunissen had relocated, so that the horse could continue his training there. Dr. Thayer testified that she stayed in close communication with Mr. Theunissen regarding Simply's training and made several trips to Georgia. Ultimately dissatisfied with Simply's progress in Georgia, the appellant brought Simply back to Wadsworth Farm in early 2007 and began regularly riding the horse herself. Dr. Thayer testified that when Simply returned to Massachusetts,

he had fundamental issues with his gait and was not developing as expected. At the time, Simply had failed to execute a "flying change," an important developmental tollgate that would have been expected of him at his age. After the horse's return to Massachusetts, the appellant requested that Lynn O'Connell prepare an assessment of Simply's marketability in April 2007 as a prelude to a potential sale where Ms. O'Connell would act as the agent. If the appellant had agreed to put the horse on the market, Ms. O'Connell would have received a commission on the ultimate sale price. Ms. O'Connell valued the horse at a market value at $40,000, a disappointingly low figure for Dr. Thayer. Ms. O'Connell then drafted a contract offering to serve as the appellant's agent in selling Simply, but recommended that Dr. Thayer try to address the major problems with the horse in order to attempt to secure a better sale price. The contract was never executed and the record does not contain any evidence that Ms. O'Connell was paid for the estimate.

Dr. Thayer testified that in June and July of 2007, as part of an effort to rebuild the horse's confidence and restart his training, she began entering Simply in dressage shows where she participated as his rider. In late July, an influential judge at one of these shows commented on Simply's performance in a written scorecard entered into evidence that read: "[b]eautiful horse, probably has soundness problems – possibly neurologic.

[Please] check." In August of 2007, the appellant testified that in response to the comment, she brought Simply to various specialists to diagnose his soundness issues. In 2008, a veterinary specialist was finally able to diagnose Simply with a structural foot problem which, once fixed, corrected his gait issues. Dr. Thayer resumed riding the horse at shows where he performed well. By the end of 2008, Simply reached level 4-3, the final level before the Prix St. George. Other than noting during her own testimony that Simply was "for sale" at the time of the hearing, the appellant did not introduce any evidence regarding whether Simply's estimated sale price had increased since Ms. O'Connell's 2007 assessment.

ii. Nautical

In 2006, the appellant purchased a second horse named "Nautical" for $29,000. Lynn O'Connell introduced the appellant to the seven-year-old horse, which had been trained by a student of Wadsworth Farm's head trainer. Ms. O'Connell and Dr. Thayer both testified that Nautical had a reputation as a difficult and wild horse, which was reflected in the low selling price. Ms. O'Connell served as the agent for the sale and brought the horse to Dr. Thayer's attention after another client of Ms. O'Connell considered buying the horse but lacked the appropriate skill necessary to ride him. Dr. Thayer testified that she had a talent for being able to ride difficult horses

that proved too challenging for others, which Ms. O'Connell corroborated in her testimony. Dr. Thayer testified that, given the difficulty others had experienced trying to ride the horse, she intended to train Nautical for two to three years after purchase in order to make him suitable to be leased to another rider. She testified that Nautical showed well and progressed through all of his training tollgates in a timely fashion. The appellant testified that Nautical was successfully leased in 2009, but did not provide any evidence as to the amount of income he later generated.

iii. Charleston 26

In May of 2007, the appellant purchased a third horse named "Charleston 26" ("Charleston") for $100,000. Lynn O'Connell was also the person that brought this horse, who was fifteen years old at the time of purchase, to the appellant's notice and served as the agent for the sale. Dr. Thayer testified that Charleston had twice won the European championships. At the time of purchase, Ms. O'Connell testified that Dr. Cesar Parra, an Olympic-level rider, had made inquiries to the seller about leasing Charleston to ride the horse at the then upcoming Pan American Games ("Pan Am Games" or "Games")— a prospect which she testified would have considerably increased the horse's value. Dr. Thayer testified that her intent was to purchase the horse and lease him to Dr. Parra. Her belief was that if Dr. Parra

took the horse with him to the Pan Am Games, it would increase the horse's value.

Dr. Thayer estimated that she could fetch a price of $500,000 for the horse if he performed well at the Games. That figure was derived in consultation with Lynn O'Connell, who based the conclusion on her knowledge of "what other horses that have gone to the Pan Am Games sell for." However, no substantive market analysis was performed and the only support given for her estimate was her testimony regarding another horse that she was familiar with, who she opined was "not as good a horse as [Charleston]," that had gone to the Pan Am Games and was for sale at the time of the hearing for $750,000. Ms. O'Connell did not give any further testimony regarding the similarities or differences between the two horses. The appellant did not offer any testimony regarding the likelihood of Charleston's success at the Games, apart from general statements regarding Dr. Parra's skill. Ms. O'Connell testified that while the Pan Am Games offered no greater competition than the events in which Charleston was already competing, the increase in value would be due to "bragging rights" and an opportunity for greater exposure to potential buyers. Ultimately, Charleston never had the opportunity to attend the Pan Am Games. While the lease agreement was being negotiated between Dr. Thayer and Dr. Parra, Dr. Parra lost his main sponsor and was thus unable to attend

the Games. Dr. Thayer testified that she consulted with an attorney regarding the lease agreement that was never executed. She testified that she received the attorney's services in return for allowing the attorney use of her horses.

Shortly after, in August of 2007, Dr. Thayer testified that Charleston had a series of "devastating medical events" involving his eye. Dr. Thayer testified that she consulted with a number of veterinary specialists, including transporting Charleston to North Carolina in February 2008 to see an eminent ophthalmologist, who was able to diagnose the horse's condition and operate using a special laser. However, Dr. Thayer testified that after the horse returned to Wadsworth Farm, there was a recurrence of issues with Charleston's eye, resulting in consultations with a number of medical specialists - - those who treat humans as well as those treating horses - - including doctors from the Massachusetts Eye and Ear Hospital in Boston. However, the appellant did not introduce any evidence indicating whether she paid for these consultations with medical doctors. Charleston required surgery under general anesthesia in August 2008, after which he spent a month in a veterinary hospital to recover. Unfortunately, the horse then developed a recurrent infection and ultimately lost use of the eye. During a procedure at Tufts Veterinary Hospital in June 2009 to replace the compromised eye with a prosthetic eye, Charleston also injured

his leg while being hoisted by the surgery team resulting in lameness.

2. Comparative Medical Consulting

On her 2008 tax return, the appellant characterized her business as a "comparative medical consultant." Dr. Thayer testified that her experiences with her horses' various medical treatments led her to realize that there was a gap between the medical knowledge and technology of veterinarians and medical doctors and specialists who treat humans. Recognizing, given her background as a surgeon, that doctors have insight that would be valuable to veterinarians, Dr. Thayer testified that she was able to connect veterinarians involved with the care of her horses to relevant specialists. The appellant did not offer any evidence as to whether she received any remuneration for these "consulting" services during the tax years at issue. The Board therefore found that these services did not constitute a different trade or business during the tax years at issue than the appellant's Simply the Best Baroch activities, which continued throughout 2008.

III. Appellant's Tax Filings and Business Records

On her Federal Form 1120, Dr. Thayer reported her income and Schedule C receipts and expenses as follows for the tax years at issue:

Tax Year	Salary	Schedule C Receipts[2]	Schedule C Expenses	Schedule C Net Income
2006	$284,121	$250	$114,368	($114,118)
2007	$300,573	$2,300	$190,326	($188,026)
2008	$304,761	$1,750	$165,972	($164,222)
Total	$889,455	$4,300	$470,666	($466,366)

The appellant has filed a Schedule C since 1998. During that time until the commencement of the tax years at issue, she reported total losses from business activities of $371,638, while she earned $1,178,559 from her employment with MGH. In sum, from the beginning of her Schedule C activity in 1998 through the end of the audit period in 2008, the appellant reported total business receipts of $11,275 and total business expenses of $849,279, resulting in total losses amounting to $838,004, at the same time that she earned $2,077,015 in wages from MGH.

During the tax years at issue, Dr. Thayer testified that she maintained an Excel spreadsheet tracking her horse-related expenses and a journal, using her credit card statements and bank account records to prepare the list. However, she did not maintain separate bank accounts for Simply the Best Baroch, paying all expenses from her personal checking account. While she did maintain a separate credit card for business matters,

[2] The appellant testified that she did not recall the source of the receipts.

Dr. Thayer testified that she often paid for personal items on her business card and paid for business items on her personal card. Dr. Thayer testified that she went over her expenses month by month, because "the expenses of the business were getting so large [that she] had to make sure that [she] could actually pay [her] mortgage" as her personal and equine expenses were all debited from the same account. The appellant testified that she maintained only one account in an effort to save on banking fees and that categorizing the expenses as equine or personal was more convenient than maintaining two accounts. The appellant provided expense records for only one of the three tax years at issue.

The appellant testified that when she purchased Simply, she prepared a job description for herself in consultation with Roel Theunissen. In that document, she described herself as "Chief Operation & Management Officer" of Simply the Best Baroch. Included among her responsibilities as laid out in the document were: (1) responsibility for overseeing the health and well-being of horses to maximize athletic performance, including overseeing the horses' medical and dental care in consultation with veterinarians; (2) responsibility for daily training and physical development of the horses six days per week; and (3) responsibility for marketing and managing the horses by entering and riding the horses in dressage shows and coordinating any

consultation with service providers. Dr. Thayer also was responsible for the purchase price and any fees incurred in connection with the horses.

Dr. Thayer created a profit projection for each of the horses that she purchased, reproduced below in simplified form. Simply and Charleston, due to their training and medical issues, did not perform according the plans set out by Dr. Thayer. The appellant did not introduce any evidence of Nautical's later performance with respect to the initial projections. The appellant did not introduce any evidence that she ever: revised future projections given changes in circumstances; adjusted the missed forecasts to reflect the actual expenses which had been incurred; or adjusted the market value of the animals. The Board also found that neither the business plans nor the projections were properly authenticated to establish that they were actually prepared, monitored, or analyzed during the years in question.

Simply the Best Profit Projection Initial Capital = $35,700				
Year	**Annual Expenses**	**Lease income**	**Sale price**	**Net profit**[3]
2003	$10,000	$0	N/A	N/A
2004	$10,000	$0	$70,000	$13,000
2005	$20,800	$0	$70,000	($7,800)
2006	$25,200	$0	$70,000	($33,000)
2007	$20,400	$0	$70,000	($53,400)
2008	$20,650	$0	$100,000	($44,050)
2009	$20,650	$0	$200,000	$35,300

Nautical Profit Projection Initial Capital = $29,000				
Year	**Annual Expenses**	**Lease income**	**Sale price**	**Net profit**
2006	$17,800	$0	N/A	($46,800)
2007	$20,400	$0	N/A	($67,200)
2008	$20,650	$0	N/A	($87,850)
2009	$17,050	$6,000	N/A	($98,900)
2010	$550	$12,000	N/A	($87,450)
2011	$550	$12,000	N/A	($76,000)
2012	$550	$12,000	N/A	($64,550)
2013	$550	$12,000	N/A	($53,100)
2014	$550	$12,000	N/A	($41,650)
2015	$550	$12,000	$50,000	$19,800

[3] The "Cost/Profit Analysis" presented by the appellant undercounted cumulative expenses in all years after the first by $500, and so correspondingly over counted potential income by that same amount. This chart reproduces the appellant's version of the numbers, with the error preserved.

Charleston Profit Projection Initial Capital = $100,000				
Year	**Annual Expenses**	**Lease Income**	**Sale price**	**Net profit**
2007	$19,130	$20,000	N/A	($99,130)
2008	$28,130	$0	$500,000	$372,740

The appellant offered into evidence a copy of the audit file of the Internal Revenue Service's ("IRS") examination of her federal returns for the tax years at issue.[4] The IRS auditor determined that the appellant was conducting Simply the Best Baroch for profit and therefore no change was made to the appellant's federal business expense deductions. As described further in the following Opinion, the Board found and ruled that the IRS auditor's determination was not dispositive for purposes of Massachusetts income tax. Furthermore, the Board found the IRS auditor's workpapers to be of limited probative value. Based on the factual record developed over two days of sworn testimony and cross examination, the Board found the appellant's lack of credibility and documentation to be much more damaging to the appellant's claims than the limited record that had been examined by the IRS auditor.

[4] The Board allowed the appellant to introduce the audit file for a limited purpose. The Board ruled that the facts and circumstances of the appellant's business as described in the audit file could have been relevant depending on the appellant's testimony in the present appeal; however, the Board ruled that it would afford the auditor's conclusions and opinions no weight. See transcript, Vol. I, p. 14.

IV. Summary of Findings

For the reasons detailed in the following Opinion, the Board found and ruled that the appellant failed to prove that her horse-related activities rose to the level of a trade or business engaged in for profit. Rather, the Board found and ruled that her involvement with horses was in the nature of a hobby which she pursued due to the recreational benefits and pleasure she derived and not from a profit-seeking motive. She was therefore not entitled to deduct her expenses related to her equine activities. Accordingly, the Board issued a decision for the appellee in this appeal.

OPINION

Massachusetts gross income is defined as federal gross income, with certain modifications not relevant to this appeal. G.L. c. 62, § 2(a). Taxpayers are permitted to deduct from that gross income "the deductions allowable under section sixty-two... of the [Internal Revenue] Code," with certain other modifications not relevant to this appeal. G.L. c. 62, § 2(d)(1). I.R.C. § 62(a)(1) allows taxpayers to take any deductions allowed under the Internal Revenue Code "which are attributable to a trade or business carried on by the taxpayer," including the deduction provided by I.R.C. § 162(a) for "all the ordinary and necessary expenses paid or incurred during the taxable year

in carrying on any trade or business." I.R.C. § 183 ("Section 183") limits I.R.C. § 162 by disallowing any trade or business deduction claimed with respect to an "activity not engaged in for profit." Accordingly, in computing Massachusetts adjusted gross income, a taxpayer may fully deduct only those expenses associated with a trade or business that was engaged in for profit. *See* ***Melecio v. Commissioner of Revenue***, Mass. ATB Findings of Fact and Reports 2013-745, 758.

I. THE ISSUE OF WHETHER THE APPELLANT WAS ENGAGED FOR MASSACHUSETTS TAX PURPOSES IN A TRADE OR BUSINESS CONDUCTED FOR PROFIT IS A QUESTION OF FACT AND LAW NOT CONTROLLED BY THE IRS AUDITOR'S DETERMINATION

The appellant argued that the IRS' determination of her federal taxable income was binding for Massachusetts tax purposes as well. While Massachusetts courts look to federal decisions under the Internal Revenue Code ("Code") to determine whether activities constitute a trade or business, ***Id.*** at 759, the Massachusetts statute permits those deductions which are "allowable" under the Code; the Commonwealth is not necessarily bound to accept "simply the dollar amount" of the determination of federal taxable income by the IRS. ***National Grid USA Service Company, Inc. v. Commissioner of Revenue,*** Mass. ATB Findings of Fact and Reports 2014-630, 643-644. Like the indebtedness at issue in ***National Grid USA Service Company, Inc.,*** the question of whether the appellant's activities constituted a trade or

business conducted for profit is a question of fact and law which the Board must "decide by weighing the appellants' facts and circumstances according to various principles...drawn from the voluminous body of Massachusetts and federal case law." ***Id.*** at 646. Further, the appellant cited no authority for the proposition that the decision of an IRS auditor that no federal tax deficiency exists is somehow binding for Massachusetts tax purposes. Therefore, the Board found and ruled that the determination of the IRS' auditor was not binding on the amount of expenses which could be deducted for Massachusetts income tax purposes and thus the Board conducted its own analysis as set forth as follows.

II. AS APPELLANT'S EQUINE ACTIVITIES WERE NOT ENGAGED IN FOR PROFIT, THE ASSOCIATED EXPENSES WERE NOT PROPERLY DEDUCTIBLE

Whether a taxpayer engages in an activity primarily for profit is a question of fact. ***Golanty v. Commissioner of Internal Revenue***, 72 T.C. 411, 426 (1979). An activity is considered to be for-profit when the individual is engaged in the activity with "the actual and honest objective of making a profit." ***Dreicer v. Commissioner of Internal Revenue***, 78 T.C. 642, 645 (1982). Greater weight is given to objective facts than to a taxpayer's "mere statement of his intent." Treas. Reg. § 1.183-2(a). "It is well-settled that the 'taxpayer bears the

burden of proving that he is entitled to claim deductions against Massachusetts income.'" ***Melecio***, Mass. ATB Findings of Fact and Reports at 2013-750(quoting ***McLaughlin v. Commissioner of Revenue***, Mass. ATB Findings of Fact and Reports 2005-538, 547).

In evaluating whether the appellant's activity was engaged in for profit, the Board looks to nine factors outlined in Treasury Regulation § 1.183-2: (1) the manner in which the taxpayer carried on the activity; (2) the expertise of the taxpayer or any advisors; (3) the time and effort expended by the taxpayer in carrying on the activity; (4) the expectation that assets used in the activity may appreciate in value; (5) the success of the taxpayer in carrying on other similar or dissimilar activities; (6) the taxpayer's history of income or losses with respect to the activity; (7) the amount of occasional profits, if any, which are earned; (8) the financial status of the taxpayer; and (9) the elements of personal pleasure or recreation. Treas. Reg. § 1.183-2(b); see ***Melecio***, Mass. ATB Findings of Fact and Reports at 2013-760. No single factor or group of factors is determinative; rather, the ultimate goal of the test is to evaluate the taxpayer's subjective intent. ***Giles v. Commissioner of Internal Revenue***, T.C. Memo 2006-15, 2006 Tax. Ct. Memo LEXIS at *21-22.

1. The Manner in Which the Taxpayer Carried on the Activity

Carrying on the activity in a "businesslike manner" is indicative that the taxpayer undertook the activity with a profit motive and can be evidenced by: maintaining complete and accurate books and records; conducting the activity in a manner similar to other similar profitable activities; and making changes to adopt new techniques or abandon unprofitable methods. Treas. Reg. § 1.183-2(b)(1). Each of those three subfactors is analyzed as follows:

a. Appellant's Books and Records

The appellant pointed to her use of separate personal and business credit cards and the maintenance of a disbursement journal for equine expenses based on her credit card expenses to demonstrate that she conducted her activities in a businesslike manner. While the Board found that Dr. Thayer did keep track of her expenses, "the significance of the business records factor lies in the use of such records for determining profitability and analyzing expenses, not merely to memorialize transactions for tax reporting purposes." ***Bronson v. Commissioner of Internal Revenue***, T.C. Memo 2012-17, 2012 Tax. Ct. Memo LEXIS at *23 (citing ***Keating v. Commissioner of Internal Revenue***, T.C. Memo 2007-309 and ***Dodge v. Commissioner of Internal Revenue***, T.C. Memo 1989-89). "Maintenance of records generally does not

indicate profit motive when there is a lack of evidence that the taxpayer used the records to improve the performance of a losing operation." ***Id.*** (citing ***Golanty,*** 72 T.C. at 430 and ***Sullivan v. Commissioner of Internal Revenue***, T.C. Memo 1998-367).

The appellant did not introduce any evidence or testimony that she used her expense records to analyze or improve the profitability of her business. Instead, the appellant testified that she used the disbursement journal to "make sure [she] could actually pay [her] mortgage" as all of the equine related expenses were paid out of the same checking account as her personal expenses, as well as to prepare her taxes. Therefore, the Board found that the appellant's tracking of her expenses was not motivated by a desire to analyze and improve profitability, but by the appellant's personal desire to simply keep track of outflows and to substantiate her tax deductions. *See* ***Giles***, 2006 Tax Ct. Memo LEXIS 14 at *25 (finding that failure to maintain records for business purposes beyond paying taxes weighed against the appellant).

Dr. Thayer testified that she prepared projections, which she claimed were produced at the time she purchased each animal, giving the estimated net profit which could be realized depending on when the horse was ultimately resold. Even assuming these projections were made contemporaneously and were reasonable at the time they were first completed, the succession

of calamities which befell Simply and Charleston after purchase and the associated expenses soon rendered them woefully inaccurate. While unforeseen circumstances may affect any business, a prudent business person would be expected to revise his or her projections to account for those circumstances. However, the appellant provided no testimony that she ever revisited her initial calculations. Therefore, the Board found that these projections did not evidence that the taxpayer conducted her activities in a businesslike manner.

The appellant further argued that her retention of test reports, show scores, medical records and horse registrations served as evidence of business-like management of her activities. However, the appellant failed to offer evidence demonstrating that this behavior differed from that of other amateur riders owning expensive horses. *See* ***Golanty***, 72 T.C. at 430 (keeping records of Arabian breeding horses is "as consistent with a hobby as it is with a business"); ***Boddy v. Commissioner of Internal Revenue***, T.C. Memo 1984-156, * 21(same). Similarly, the Board found that nothing included in the appellant's self-prepared job description exceeded the activities expected of an amateur horse owner.

The Board found that while the appellant maintained records, they were not used to evaluate and improve the overall performance of her equine activity. Therefore, the Board found

that this subfactor weighed in favor of the appellee.

Following practices of comparable businesses

Where an activity is carried on in a manner substantially similar to other activities of the same nature which are profitable, a profit motive may be indicated. Treas. Reg. § 1.183-2(b)(1). Lynn O'Connell, who operated her own equine business, testified that she believed the appellant's purchases to be sensible at the time they were made and the appellant testified that she spoke with Roel Theunissen in initially putting together her profit projections. However, no evidence or testimony was offered as to whether Dr. Thayer carried on her equine activities in a manner that another profitable horse business might have done in similar circumstances. Therefore, this subfactor was neutral.

b. Changes to business operations

When a taxpayer changes operating methods, adopts new techniques, or abandons unprofitable methods in a manner consistent with an intent to improve profitability, a profit motive may be indicated. ***Id.*** Dr. Thayer faced many challenges with her horses that she had to react to -- namely, Simply's training issues and Charleston's eye injuries. The Board found that Dr. Thayer did an admirable job at directing their care and responding to medical crises as they arose; however, the Board found that the appellant did nothing to improve profitability.

The appellant argued that her decision not to sell Simply once presented with Ms. O'Connell's sales estimate demonstrated such an abandonment of unprofitable methods with an intent to improve profitability. However, despite having subsequently fixed the training issues with the horse, the appellant presented no evidence regarding the possibility of generating a profit from the horse, whether by sale, lease, or other use. After Simply failed to produce the results hoped for and instead generated a rising stream of expenses with no income to offset them, the appellant purchased Nautical, a horse that could not be leased for years until he was properly trained. The purchase of Charleston followed, from which the appellant anticipated $20,000 of lease revenue, barely enough to cover the expenses from that horse alone for the year. This was to be followed by a quick five-fold return on investment, banking on an assumption that the horse would perform well at the Pan Am Games, the likelihood of which the appellant failed to substantiate. The Board therefore found that the appellant did not present any evidence that she sufficiently adapted her business model to reflect the impact from the significant losses incurred year after year due to costly medical interventions and training.

The Board found that this subfactor therefore weighed in favor of the appellee and thus, the first factor as a whole weighed in favor of the appellee.

2. Expertise of the Taxpayer or Any Advisors

A taxpayer's expertise, research, and study of an activity, as well as his or her consultation with experts, may be indicative of a profit motive. Treas. Reg. § 1.183-2(b)(2). While the appellant has many years of experience riding and training horses, the focus of this factor is upon "expertise and preparation with regard to the economic aspects of the particular business, and failure to possess or obtain expertise in this area will not be excused by study of other aspects of the activity or by general business acumen." ***Hastings v. Commissioner of Internal Revenue***, T.C. Memo 2002-310, 2002 Tax Ct. Memo LEXIS 331 at *18 (emphasis added); *See* ***Golanty***, 72 T.C. at 432; ***Melecio***, Mass. ATB Findings of Fact and Reports at 2013-764. "While a formal market study is not required, a basic investigation of the factors that would affect profit is." ***Burger v. Commissioner of Internal Revenue***, T.C. Memo 1985-523; 1985 Tax Ct. Memo LEXIS 107 at *19. Furthermore, taxpayers should not only familiarize themselves with the undertaking, but should also "consult or employ an expert, if needed, for advice on how to make the operation profitable." ***Burger v. Commissioner of Internal Revenue***, 809 F.2d 355, 359 (1987); ***Golanty***, 72 T.C. at 432.

There is little indication in the record that the appellant made any serious effort to develop expertise in the economics of

training, leasing and selling horses as a business. The appellant argued that her consultations with various professionals demonstrated that she availed herself of the expertise of others in carrying on her activity. The Board found, however, that the lack of record keeping and lack of payment for these "consultations" was not indicative of a *bona fide* business relationship. In addition, her consultations with accountants were limited to the preparation of tax returns.

Similarly, the appellant failed to present evidence tending to distinguish her consultations with Wadsworth Farm's owner and head trainer regarding the purchase and sale of her horses from those of an ordinary high-level amateur rider. Ms. O'Connell testified that she did not assist with the preparation of Dr. Thayer's profit projections. While Ms. O'Connell and Dr. Thayer consulted often about matters of the horses' training and wellbeing, Ms. O'Connell did not give any testimony that she advised the appellant with respect to the business of profitably training and selling horses. Accordingly, the Board found that the appellant lacked any expertise in the economics of the equine business and failed to obtain the requisite counsel to ensure her activities were profitable. *See* ***Dodge***, 1998 Tax Ct. Memo LEXIS 89 at *16 (finding that a taxpayer's expertise in horse breeding in the absence of expertise in the economics of running a horse breeding business or consulting experts for

business advice did not support the taxpayer's case).

Therefore, the Board found that this factor weighed in favor of the appellee.

3. The Time and Effort Expended by the Taxpayer

If the taxpayer devotes much of his or her personal time and effort to conducting an activity, this may indicate a profit motive, particularly if the activity lacks "substantial personal or recreational aspects." Treas. Reg. § 1.183-2(b)(3); ***Golanty***, 72 T.C. at 415. However, the fact that the taxpayer devotes only a limited amount of time to an activity does not necessarily indicate a lack of profit motive where the taxpayer employs competent and qualified persons to carry on such activity. ***Id.***

The appellant estimated that she spent 25-29 hours per week on her equine activity. While the effort was not full time due to her demanding professional schedule, such an amount of time is not incompatible with a profit motive. However, based on the appellant's testimony, that time was predominantly spent training and riding the horses, performing in shows, and attending to the horses' medical care. The Board found that these tasks would have been performed whether the activity was undertaken primarily for profit or as a hobby. Furthermore, the fact that the appellant has owned, trained, and ridden horses her entire life indicates that the activity had "substantial personal or recreational aspects" other than a profit motive.

Similarly to the appellant, the taxpayer in ***Giles*** was a successful dentist as well as a life-long equestrian. 2006 Tax Ct. Memo LEXIS at *2-*5. Although she managed her own full-time dental practice, she spent up to six hours a day riding and caring for her Arabian horses, which she also bred. ***Id.*** at *5-*6. The Tax Court held that while "personal pleasure derived from an activity will not turn a business into a hobby," the fact that the taxpayer had enjoyed riding and showing horses since childhood indicated that she would have spent similar time with her horses as an amateur rider. ***Id.*** Therefore, since the activity had significant personal and recreational benefits, the Tax Court gave this factor no weight in its analysis as to whether Ms. Giles operated her activity for profit. ***Id.***

The Board found that although the appellant devoted significant time to her horses, because of the appellant's keen interest in equestrianism, she would have spent that time regardless of whether she intended to carry on a trade or business. Therefore, like the Tax Court in ***Giles***, the Board found this factor to be neutral.

4. The Expectation that Assets May Appreciate in Value

Even if no profit is derived from current operations, a taxpayer may intend to derive a profit from operation of an activity where an overall profit will result when appreciation of an asset exceeds expenses of operation. Treas. Reg. § 1.183-

2(b)(4). The appellant's profit projections for each horse anticipated an appreciation in the horses' value sufficient to generate a profit when sold. Even taking the appellant's projections at face value, Dr. Thayer anticipated $254,160 of expenses for all three horses from 2003 to 2015 and only $98,000 of income during the same period for an overall operating loss of $156,160. Unfortunately, in actuality, the operating loss for the three tax years at issue alone amounted to $466,366. This was in addition to the $371,638 of losses already incurred before the tax years at issue.

Dr. Thayer's only hope for turning a profit was to earn large returns on the sales of her horses. From a purchase price of $37,500, Dr. Thayer predicted Simply would generate a sale price of $200,000 in 2009 or a profit of $162,500 or 433%. However, as late as April 2007, Ms. O'Connell, after an extensive analysis, estimated Simply's market value at $40,000, or only $2,500 more than she had paid five years previously. While Dr. Thayer testified that Simply improved after that sales analysis was done, she failed to provide the Board with any evidence to support an increased valuation of the horse.

Dr. Thayer testified that she purchased Charleston for $100,000 with the intention that he could be quickly sold for $500,000 after a performance at the Pan Am Games. This valuation

by Ms. O'Connell was not supported by a written sales analysis such as the one she had done for Simply. Instead, the Board found this estimate to be conjecture based on anecdotal evidence of the intangible value of "bragging rights" and the sale price of one other horse without attendant analysis of its comparability to Charleston.

Even if Dr. Thayer could have earned "a substantial profit with one outstanding horse[,] [t]he possibility of a speculative profit in a taxpayer's horse activity ... is insufficient to outweigh the absence of profits for a sustained period of years." ***Foster v. Commissioner of Internal Revenue***, T.C. Memo 2012-207, 2012 Tax. Ct. Memo LEXIS 209 at *22. If Dr. Thayer had been able to sell Charleston for $500,000 in 2007 after the Games, that $400,000 profit plus the $2,500 profit she could have earned at the time on Simply would still have been insufficient to offset the operating losses she had incurred up until that point. Therefore, the Board found that this factor weighed strongly in favor of the appellee.

5. The Taxpayer's Success in Carrying On Other Similar or Dissimilar Activities

The fact that a taxpayer previously engaged in similar activities and converted them from unprofitable to profitable enterprises may indicate that he or she is engaged in the present activity for profit, even though the activity is

presently unprofitable. Treas. Reg. § 1.183-2(b)(5). Although the appellant has long ridden and trained horses, she has never generated a profit from any of her equine activities, since she began reporting them in 1998. Further, while the appellant was a successful doctor and director of a large research laboratory during and before the tax years at issue, she failed to show that she conducted her equine activity in a similarly businesslike manner. Therefore, the Board found that this factor was neutral. *See* ***Giles***, 2006 Tax. Ct. Memo 14 at *45 (taxpayer's successful dental practice was not indicative of conducting her horse activities in a businesslike manner).

6. The Taxpayer's History of Income or Loss from the Activity

"Although no one factor is determinative of the taxpayer's intention to make a profit, a record of substantial losses over many years and the unlikelihood of achieving a profitable operation are important factors bearing on the taxpayer's true intention." ***Golanty***, 72 T.C at 426 (internal citation omitted). If losses are sustained because of "unforeseen or fortuitous circumstances which are beyond the control of the taxpayer" the losses are not to be taken as an indication that the activity is not engaged in for profit. Treas. Reg. § 1.183-2(b)(6). The sickness or injury of horses is considered to be the kind of fortuitous circumstances contemplated in that definition.

Engdahl v. Commissioner of Internal Revenue, 72 T.C. 659, 669 (1979); ***Bronson v. Commissioner of Internal Revenue***, T.C. Memo 2012-17, 2012 Tax Ct. Memo LEXIS 18 at *29-*30.

The appellant claimed that she was still in the "start-up phase" of her business activities. The "presence of losses in the formative years of a business, particularly one involving the breeding of horses, is not inconsistent with an intention to achieve a later profitable level of operation, bearing in mind, however, that the goal must be to realize a profit on the entire operation, which presupposes not only future net earnings but also sufficient net earnings to recoup the losses which have meanwhile been sustained in the intervening years." ***Bessenyey v. Commissioner of Internal Revenue,*** 45 T.C. 261, 274 (1965); *see also* I.R.C. § 183(d) and Treas. Reg. § 1.183-2(b)(6). However, Dr. Thayer did not provide any evidence as to the likelihood that future earnings will be sufficient to cover not only her expenses but to offset the substantial losses she has already sustained. As previously discussed, the Board found that possibility to be remote during the tax years at issue.

However, because the fact that the appellant has not demonstrated her future potential for profit is countervailed by the fact that the losses during the tax years at issue were incurred in the early years of operation and were driven by unforeseen medical events, the Board found that this factor was

neutral. *See* ***Hastings***, 2002 Tax Ct. Memo LEXIS 331 at *22-*23 (factor was neutral where taxpayer could not demonstrate that future income would overcome start-up losses).

7. Amount of Occasional Profits

The amount of profits in relation to the substantial amount of losses incurred and in relation to the amount of the taxpayer's investment are criteria in determining the taxpayer's intent. Treas. Reg. § 1.183-2(b)(7). During the tax years at issue, the appellant only reported $4,300 of receipts from her equine activity, the source of which she could not recall, and she has never generated a profit. The Board found that this factor thus weighed heavily in favor of the appellee.

8. The Taxpayer's Financial Status

Substantial income from sources other than the activity in question may indicate that the taxpayer is not engaged in the activity for profit, particularly if the losses generate substantial tax benefits or there are personal or recreational elements involved. Treas. Reg. § 1.183-2(b)(8); ***Engdahl***, 72 T.C. at 666-68. "The limitations in IRC § 183 are 'designed to prevent taxpayers from offsetting unrelated income with losses from an activity not carried on for profit.'" ***Melecio***, Mass. ATB Findings of Fact and Reports at 2013-766 (quoting ***Magassy v. Commissioner of Internal Revenue***, T.C. Memo 2004-4; 2004 Tax Ct. Memo LEXIS 2 at *27). During the tax years at issue, the

appellant was employed as a surgeon, professor, and research laboratory director, earning $284,121, $300,573 and $304,761 in 2006, 2007, and 2008, respectively. During the same time period, the appellant reported net losses from her equine activity of $114,118, $188,026 and $164,223, respectively, thereby substantially reducing her taxable income. The Board found that Dr. Thayer's work as a doctor subsidized her equine activities and the mountain of expenses that they generated. Without her salary from MGH, these expenses would have needed to be funded out of the paltry $4,300 of revenue that the equine business generated. *See* ***Golanty***, 72 T.C. at 428-429 (weighing this factor against a doctor whose salary "was substantial and was sufficient to enable [him and his wife] to maintain a comfortable standard of living notwithstanding the losses from the[ir] horse-breeding operation"); ***Giles***, 2006 Tax Ct. Memo LEXIS 14 at *52 (weighing this factor against a dentist earning a high salary given the significant reduction in after-tax cost due to proposed deductions).

The Board therefore found that this factor weighed heavily in favor of the appellee.

9. The Elements of Personal Pleasure or Recreation

Deriving enjoyment from the particular activity at issue may indicate that the taxpayer is not conducting the activity for profit, though the presence of a personal or recreational

element is not determinative if a profit motive is evidenced by other factors. Treas. Reg. § 1.183-2(b)(9). "Unquestionably, an enterprise is no less a 'business' because the entrepreneur gets satisfaction from his work; however, where the possibility for profit is small (given all the other factors) and the possibility for gratification is substantial, it is clear that the latter possibility constitutes the primary motivation for the activity." ***Burger***, 1985 Tax Ct. Memo LEXIS 107 at *26; ***Bessenyey***, 45 T.C. at 275.

The appellant has been an avid horse rider since her youth. The Board found it clear from her testimony that even though keeping horses involves significant effort, Dr. Thayer received great personal reward, despite of the entire lack of monetary reward, from the sport of dressage and from her relationships with her animals. While working grueling hours at MGH, the appellant still made time to train and ride her horses. She testified that she generally had not taken vacation other than to work with those horses. Dedication can be "equally demonstrative of a commitment to the horses themselves and an inclination to work with them as it is of a profit making intent." ***Eastman v. United States***, 225 Ct. Cl. 298, 306-307 (1980).

The Board found Dr. Thayer, because of her life-long personal interest in horse riding and training, would have

continued her activity regardless of its profitability and thus this factor weighed strongly in favor of the appellee.

CONCLUSION

Having considered the above factors, recognizing that no one factor is controlling, and analyzing the record as a whole, the Board found and ruled that the appellant did not meet her burden of proving that she was engaged in her equine activity with the profit objective required and that she therefore was not entitled to deduct the expenses associated with her activity as a business expense. The Board accordingly issued a decision for the appellee in this appeal.

THE APPELLATE TAX BOARD

By: _____
Thomas W. Hammond, Jr., Chairman

A true copy:

Attest: _____
Clerk of the Board