

## WHOLESALE CLUB PURCHASES CAN BE DEDUCTIBLE, BUT...

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A semi-secret of many restaurants and stores is that a large part of their ingredients and inventory of items for sale are purchased at wholesale clubs, such as Costco and Sam's Club. Such purchases are a testament to the favorable prices available at such clubs that are available to both businesses and individual shoppers.

There is nothing that prohibits a taxpayer from expensing items purchased from such clubs, or adding them to cost of goods sold for purposes of determining income from sale of inventory. However, there is a right way and wrong way to go about this. A recent Tax Court case illustrates the wrong way.

In the case, the taxpayers, who ran two restaurants, included in their cost of goods sold items purchased from grocery stores and wholesale clubs. They produced photocopied receipts from the stores to substantiate their expenses. In upholding the IRS in disallowing a large part of these deductions, the Tax Court noted:

These receipts are of little value. Without an explanation from the Daouds, it is impossible for us to distinguish items used at their Wienerschnitzels from those used by them personally. Many of the items on the receipts are household or personal care products, or food and drink (e.g., liquor) that we find were probably not served or used at their restaurants.

Some simple lessons can be gleaned. First, detail on the receipts what was purchased. Second, don't combine personal items on the same receipts as business items.

It didn't help the taxpayers that there were a multitude of other facts and issues detailed in the case that raised numerous questions for the Court as to the accuracy of the taxpayers' returns, perhaps coloring the Court's opinion of the taxpayers' claims that the receipts substantiated bona fide business items.

*Daoud*, TC Memo 2010-282

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