Fred Draper, et al., Petitioners, v. Commissioner of Internal Revenue, Respondent, 32 T.C. 545 (1959)</p>

A taxpayer’s good-faith reliance on professional advice can negate the intent to evade taxes, impacting the application of the statute of limitations and potential penalties, and contributions to a trust created for the construction and operation of a building to be used exclusively by domestic fraternal societies operating under the lodge system and exclusively for religious, charitable, scientific, literary, or educational purposes qualify as charitable contributions.

Summary</p>

In this U.S. Tax Court case, the Commissioner of Internal Revenue determined deficiencies and additions to tax against Fred and Carrie Draper. The issues involved were whether the loss from a destroyed storage building qualified under Section 117(j) of the 1939 Internal Revenue Code, the deductibility of contributions to the Draper Trust as charitable donations, whether a significant portion of gross income had been omitted, triggering a longer statute of limitations, the effect of a payment made in anticipation of a tax liability, and whether Fred Draper filed false and fraudulent tax returns. The court addressed these issues, finding for the Commissioner on some points, but, notably, holding that Fred Draper’s reliance on his accountant, post-1944, negated a finding of fraudulent intent, and for the Drapers on the charitable contribution deductions.

Facts</p>

Fred Draper operated a lumber company, with Carrie assisting in the office until their separation in 1943. In 1949, a briquette storage building, under construction for several months, was destroyed by windstorm. Draper formed the Draper Trust in 1948 to construct a building for use by fraternal societies and religious, charitable, and educational purposes and made contributions to this trust in 1948 and 1949. Fred Draper intentionally omitted income from the business’s records from 1944 onward to avoid sharing profits with Carrie. He then consulted with accountants who were aware of the unreported income. Amended returns were eventually filed, and a criminal tax evasion case was brought against Fred. A substantial sum was paid to the IRS in anticipation of a tax liability that had not yet been assessed. The Drapers filed timely separate returns for 1944, and Fred omitted substantial income from tax returns from 1945 to 1948.

Procedural History</p>

The Commissioner determined tax deficiencies and penalties for the Drapers. The Drapers appealed to the U.S. Tax Court. The Tax Court heard the case. The court ruled on each issue, finding for the Commissioner on some issues, but finding for the Drapers on the deductibility of contributions to the trust and finding that the statute of limitations applied to some years because of a lack of fraudulent intent.

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Issue(s)</p>

1. Whether the loss on the destroyed storage building should be subject to Section 117(j) of the Internal Revenue Code of 1939, thereby affecting the amount of the deductible loss.
2. Whether contributions to the Draper Trust were deductible as charitable contributions under Section 23(o) of the Internal Revenue Code of 1939.
3. Whether omissions from gross income exceeded 25% of the reported income, thus extending the statute of limitations under Section 275(c) of the 1939 Code.
4. Whether a payment made to the IRS in anticipation of a potential tax deficiency, and placed in a suspense account, constituted a payment of tax.
5. Whether Fred Draper filed false and fraudulent income tax returns with intent to evade tax, thereby impacting the statute of limitations.

Holding</p>

1. Yes, because part of the building's construction was complete more than six months before its destruction, the loss was subject to the offsetting rules of Section 117(j).
2. Yes, because the trust was to be used exclusively for charitable purposes, contributions were deductible.
3. Yes, for Carrie, because Fred's return could not be considered. No, for Fred, because he had fraudulent intent in 1944.
4. No, because no tax had been assessed or allocated to the payment of a tax, it was not a payment of tax.
5. Yes, for 1944 only, because the intent to evade tax was present. No, for 1945-1948, because after 1944, Fred's reliance on accountants negated an intent to evade.

Court's Reasoning</p>

The court applied the plain language of the tax code to determine the deductibility of the casualty loss under section 117(j), finding that the holding period began when construction began, overruling its prior decision in M.A. Paul. The court held that the Draper Trust qualified as a charitable organization based on the exclusive charitable purpose outlined in the trust agreement, following section 23(o) of the 1939 Code. Regarding the statute of limitations, the court distinguished between the Drapers. The court found that Carrie Draper had not included all the income, and therefore, the statute of limitations could be extended on the grounds of unreported income. The court considered that Fred had a good-faith reliance on professional advice as a defense. The court cited Rosenman v. United States to determine that the payment to the IRS was not a payment of tax because it had not been applied to a specific tax liability. The court looked at Fred's intent and conduct to determine if his returns were fraudulent. While Fred intentionally hid income in 1944 with the purpose of evading taxes, this changed in

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1945. The court reasoned that Fred, after 1944, did not intentionally hide income because he discussed this with his accountants, and showed his intent to report the income and pay the taxes due by seeking professional assistance. The court quoted "a taxpayer cannot thus relieve himself of the responsibility to file correct and accurate tax returns."

Practical Implications</p>

This case underscores the importance of maintaining accurate financial records and the implications of taxpayer intent in tax cases, especially as it relates to the statute of limitations. It highlights that reliance on professional advice, while not a complete defense, can be crucial in negating the element of fraudulent intent. The decision emphasizes that a taxpayer’s actions and communications with tax professionals are central to the determination of intent. This case also clarifies that, for the purposes of a statute of limitations determination based on omitted income, a spouse’s return cannot be considered when determining the gross income on another spouse’s return. This is a crucial consideration in community property states. Finally, it demonstrates the court’s willingness to examine the substance of the facts and evidence of intent, rather than merely the form or superficial elements of the tax returns.

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