***Estate of William F. L. Fry, Deceased, Dauphin Deposit Bank & Trust Company, Coexecutor, and Grace H. Fry, Petitioners v. Commissioner of Internal Revenue, Respondent, 88 T. C. 1020 (1987)***

A taxpayer's disclosure on a tax return must adequately apprise the IRS of the nature and amount of a transaction to invoke the exception to the six-year statute of limitations.

**Summary**

In Estate of Fry v. Commissioner, the IRS issued a notice of deficiency over three years after the taxpayers filed their 1976 return, relying on the six-year statute of limitations due to omitted income. The taxpayers argued that their disclosure on the return should trigger the exception under IRC § 6501(e)(1)(A)(ii). The Tax Court held that the taxpayers' disclosure was insufficient and misleading, thus the six-year statute applied. The case emphasizes the need for clear and comprehensive disclosures on tax returns to avoid extended audit periods.

**Facts**

In 1976, William Fry, a certified public accountant, and his wife, Grace Fry, reported a stock sale transaction on their tax return. The transaction involved the sale of Fry's shares in Smith Land & Improvement Corp. to the corporation itself for $1,150,000, with an initial payment of $150,000 in the form of a land parcel. The return stated the sale price, cost basis, and gain realized, but did not specify that the payment was in property or that it was a redemption by a closely held corporation.

**Procedural History**

The IRS issued a notice of deficiency on June 20, 1983, for the 1976 tax year, which was more than three years after the return was filed but within six years. The taxpayers moved for partial summary judgment, arguing the disclosure on their return invoked the three-year statute of limitations under IRC § 6501(e)(1)(A)(ii). The Tax Court denied the motion, finding the disclosure inadequate.

**Issue(s)**

1. Whether the disclosure on the taxpayers' 1976 tax return was sufficient to apprise the IRS of the nature and amount of the omitted income under IRC § 6501(e)(1)(A)(ii).

**Holding**

1. No, because the disclosure on the return was insufficient and misleading, failing to indicate that the transaction was a redemption by a closely held corporation or that payment was made in property rather than cash.

 

## Court’s Reasoning

The Tax Court applied the rule from IRC § 6501(e)(1)(A)(ii), which requires a disclosure adequate to inform the IRS of the nature and amount of an omitted item. The court noted that the purpose of the six-year statute is to address situations where the return does not provide clues to omitted income, as established in Colony, Inc. v. Commissioner. The court found the Fry’s disclosure misleading because it described the transaction as a cash sale rather than a redemption involving property. The court emphasized that such transactions between a corporation and its shareholders require special scrutiny and should be clearly disclosed. The court also cited Benderoff v. United States, stating that disclosures must be detailed enough to inform the IRS’s decision on whether to audit. The court concluded that the taxpayers’ disclosure did not meet the statutory requirement, thus the six-year statute applied.

## Practical Implications

This decision underscores the importance of detailed and accurate disclosures on tax returns. Taxpayers must ensure that disclosures of transactions, especially those involving closely held corporations and non-cash payments, are clear and comprehensive to avoid triggering the extended statute of limitations. Legal practitioners should advise clients on the necessity of full disclosure to prevent prolonged IRS scrutiny. The ruling has implications for how similar cases involving redemption transactions and omitted income are analyzed, potentially affecting business practices related to corporate transactions and tax reporting. Subsequent cases, such as Thomas v. Commissioner and University Country Club, Inc. v. Commissioner, have further clarified the requirements for adequate disclosure, but Estate of Fry remains a key reference for understanding the application of the six-year statute of limitations.