128 T.C. 37 (2007)

The statute of limitations for assessing income tax is indefinitely extended when a tax return is fraudulent, even if the fraud was committed by the return preparer without the taxpayer's knowledge or intent to evade tax.

Summary

Vincent Allen hired Gregory Goosby to prepare his tax returns for 1999 and 2000. Goosby fraudulently inflated deductions on Allen's returns with the intent to evade tax, though Allen himself lacked such intent. The IRS issued a deficiency notice to Allen after the standard three-year statute of limitations had expired, arguing that the fraudulent return extended the limitations period indefinitely under 26 U.S.C. § 6501(c)(1). The Tax Court held that the statute's plain language extends the limitations period for fraudulent returns regardless of who perpetrated the fraud, thus allowing the IRS to assess the deficiency.

Facts

Petitioner Vincent Allen hired tax preparer Gregory Goosby to prepare his 1999 and 2000 tax returns.

Goosby fraudulently inflated itemized deductions on Allen's Schedule A for both years, including charitable contributions, meals, entertainment, and other expenses.

These fraudulent deductions were made with the intent to evade tax.

Allen received copies of the filed returns but did not file amended returns.

Goosby was later convicted of willfully aiding in the preparation of false tax returns under 26 U.S.C. § 7206(2), though not specifically based on Allen's returns.

The IRS issued a deficiency notice to Allen on March 22, 2005, after the normal 3-year statute of limitations had expired for both 1999 and 2000 returns.

Allen conceded the disallowed deductions but contested the timeliness of the deficiency notice.

Both parties stipulated that the returns were fraudulent due to Goosby's actions, but Allen himself did not intend to evade tax.

Procedural History

The IRS issued a deficiency notice to Vincent Allen.

Allen petitioned the Tax Court, contesting the deficiency notice as untimely due to the expiration of the statute of limitations.

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The case was submitted to the Tax Court fully stipulated.

The Tax Court issued an opinion in favor of the Commissioner of Internal Revenue, upholding the deficiency notice.

Issue(s)

1. Whether the statute of limitations for assessing income tax under 26 U.S.C. § 6501(c)(1) is extended indefinitely when a return is "false or fraudulent with the intent to evade tax," if the fraudulent intent is solely that of the return preparer, not the taxpayer.

Holding

1. Yes. The Tax Court held that the statute of limitations is extended indefinitely because the plain language of 26 U.S.C. § 6501(c)(1) refers to a "false or fraudulent return," not to whose fraud caused the return to be false.

Court's Reasoning

The court began with the plain language of 26 U.S.C. § 6501(c)(1), which states that in the case of "a false or fraudulent return with the intent to evade tax," the tax may be assessed at any time. The court emphasized that the statute does not explicitly require the fraud to be that of the taxpayer.

The court noted that statutes of limitations are generally construed strictly in favor of the government, citing *Badaracco v. Commissioner, 464 U.S. 386, 391 (1984)*. The purpose of the extended limitations period for fraudulent returns is to address the "special disadvantage to the Commissioner in investigating these types of returns," as three years may be insufficient to uncover fraud.

The court reasoned that this disadvantage exists regardless of whether the fraud is committed by the taxpayer or the preparer. Allowing the statute of limitations to expire in cases of preparer fraud would permit taxpayers to benefit from fraudulent returns simply by claiming ignorance of the fraud.

The court rejected Allen's argument that extending the limitations period based on preparer fraud would be unfairly burdensome, stating, "Taxpayers are charged with the knowledge, awareness, and responsibility for their tax returns." The ultimate responsibility to file accurate returns and pay taxes rests with the taxpayer, not the preparer.

The court distinguished cases cited by Allen, which involved the fraud penalty under 26 U.S.C. § 6663, noting that those cases focused on taxpayer fraud because the penalty was being asserted against the taxpayer. Those cases did not limit the definition of fraud under § 6501(c)(1) exclusively to taxpayer fraud.

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The court concluded that because the returns were stipulated to be fraudulent due to the preparer's intent to evade tax, the indefinite statute of limitations under § 6501(c)(1) applied, and the deficiency notice was timely.

Practical Implications

Allen v. Commissioner clarifies that the extended statute of limitations for fraudulent tax returns applies even when the taxpayer is unaware of the fraud perpetrated by their preparer. This ruling places a significant burden on taxpayers to diligently oversee their tax preparation and review returns for accuracy, even when relying on professionals.

For legal practitioners, this case underscores the importance of advising clients to actively engage in the tax preparation process and to independently verify the accuracy of their returns. It also highlights that ignorance of preparer fraud is not a shield against extended IRS scrutiny and potential tax liabilities.

This decision reinforces the IRS's ability to pursue tax deficiencies discovered beyond the typical three-year window when fraud is present in the return, irrespective of the taxpayer's direct involvement in the fraudulent activity. It signals a broad interpretation of "fraudulent return" under 26 U.S.C. § 6501(c)(1) that focuses on the nature of the return itself rather than solely on the taxpayer's intent.

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