Barkett v. Commissioner, 143 T. C. 6 (U. S. Tax Court 2014)

In Barkett v. Commissioner, the U. S. Tax Court upheld the six-year statute of limitations for tax assessments when taxpayers omit more than 25% of their gross income. The court ruled that for investment sales, only the gain, not the total proceeds, counts as gross income for this purpose, aligning with prior decisions and rejecting the taxpayers' argument to include total proceeds. This decision reaffirms the legal standard for determining gross income in tax deficiency cases, impacting how taxpayers report investment sales.

Parties

G. Douglas Barkett and Rita M. Barkett, petitioners, challenged the Commissioner of Internal Revenue, respondent, over a notice of deficiency concerning their federal income tax for the taxable years 2006 to 2009.

Facts

The Barketts filed their 2006 and 2007 tax returns on September 17, 2007, and October 2, 2008, respectively. They reported gains from the sale of investments amounting to approximately $123,000 in 2006 and $314,000 in 2007, but the total amounts realized from these sales were more than $7 million and $4 million, respectively. The Commissioner sent a notice of deficiency on September 26, 2012, alleging the Barketts omitted gross income of $629,850 in 2006 and $431,957 in 2007, unrelated to the investment sales. The Barketts contested the notice's validity, arguing it was sent beyond the three-year statute of limitations under I. R. C. sec. 6501(a). The Commissioner countered that the six-year limitations period under I. R. C. sec. 6501(e) applied due to the Barketts' omission of more than 25% of their gross income.

Procedural History

The Barketts filed a petition with the U. S. Tax Court seeking partial summary judgment. The Tax Court considered the motion under Rule 121(a) of the Tax Court Rules of Practice and Procedure. The court reviewed prior decisions and the statutory framework to determine the applicable limitations period.

Issue(s)

Whether the six-year statute of limitations under I. R. C. sec. 6501(e) applies to the Barketts' 2006 and 2007 tax returns when they omitted gross income exceeding 25% of the gross income stated in their returns, calculated as gains from the sale of investment property rather than the total amounts realized?

Rule(s) of Law

Under I. R. C. sec. 6501(a), the IRS must assess tax or send a notice of deficiency

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within three years after a return is filed. However, I. R. C. sec. 6501(e)(1) extends this period to six years if the taxpayer omits from gross income an amount properly includible therein that exceeds 25% of the gross income stated in the return. I. R. C. sec. 61(a) defines gross income as "all income from whatever source derived," including "[g]ains derived from dealings in property. "

Holding

The Tax Court held that the six-year statute of limitations under I. R. C. sec. 6501(e) applies to the Barketts' 2006 and 2007 tax returns because the omitted gross income exceeded 25% of the gross income stated in their returns, calculated as the gains from the sale of investment property rather than the total amounts realized.

Reasoning

The court reasoned that the Home Concrete & Supply, LLC decision, which invalidated a portion of a regulation concerning omitted gross income, did not affect the calculation of gross income as gains from investment sales. The court cited prior cases, such as Insulglass Corp. v. Commissioner and Schneider v. Commissioner, which established that gross income for the purpose of I. R. C. sec. 6501(e) includes gains, not the total proceeds, from the sale of investment property. The court also noted that the Home Concrete decision's dictum supported this interpretation, as it explained gross income as the difference between the amount realized and the cost of the property sold. The court rejected the Barketts' argument that the total proceeds from investment sales should be considered gross income, emphasizing that the exception in I. R. C. sec. 6501(e)(1)(B)(i) for trade or business income did not apply to their investment sales. The court's analysis focused on statutory interpretation, prior case law, and the specific facts of the Barketts' case, ultimately upholding the six-year statute of limitations.

Disposition

The Tax Court denied the Barketts' motion for partial summary judgment, affirming that the six-year statute of limitations applied to their 2006 and 2007 tax years, making the Commissioner's notice of deficiency timely.

Significance/Impact

Barkett v. Commissioner reinforces the interpretation of "gross income" under I. R. C. sec. 6501(e) for investment sales, impacting how taxpayers report such income and the IRS assesses deficiencies. The decision clarifies that only gains, not total proceeds, are considered for determining the applicability of the six-year statute of limitations, aligning with prior case law and statutory definitions. This ruling provides guidance for taxpayers and practitioners in calculating gross income for statute of limitations purposes, potentially affecting future tax litigation and compliance strategies.

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