

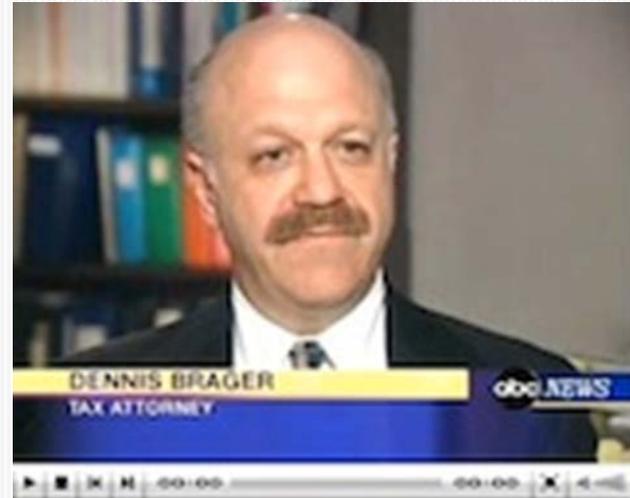


Innocent Spouse Relief: Fact or Fiction?

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Three Types of Relief



- Traditional Innocent Spouse Relief- IRC Section 6015(b)
- Spousal Allocation. IRC Section 6015(c)
- Equitable Relief. IRC Section 6015(f)

A Few Common Denominators



- A joint tax return
 - Generally if one spouse's signature was forged no joint return exists, BUT consider implications of community property laws.
 - Joint tax return may exist even if one spouse didn't sign
- Applies only to income tax
 - Not e.g. TFRP , or FBAR penalties
- A timely election on Form 8857
 - Timing under IRC Sections 6015(b) and (c).
 - Election must be made within two years of IRS first collection activity.
 - Collection activity includes the offset by the IRS of a tax refund of the requesting spouse
 - Timing Under IRC Section 6015(f)
 - Generally within the Statute of Limitations on Collection, i.e. 10 years.

Spousal Allocation.



IRC Section 6015(c)

- An electing spouse may allocate any tax deficiency in proportion to each spouse's contribution to the deficiency.
 - The allocation is made without regard to community property laws.
 - No refunds are permitted
 - Election may be made only by an individual who at the time of the election is no longer married, or is legally separated from the other spouse, or who is not a member of the same household during the 12 month period ending on the date the election is filed.
- If the IRS demonstrates that the individual making the election had actual knowledge at the time the return was signed then relief is not available. The burden of proof is on the IRS.
- Actual knowledge- NOT reason to know
- Actual knowledge of what? See *Chesire v. Commissioner*, 115 T.C. 183 at 195; *King v. Commissioner*, 116 T.C. 198 (2001).

Traditional Innocent

Spouse Relief IRC Section 6015(b)

- Most difficult form of relief to obtain
- Requires that in signing the return, the requesting spouse did not know or had no reason to know there was an understatement on the return
- Not available in “non-payment” cases
 - Only available for deficiency cases
- It is rare that a client would qualify under Section 6015(b), but not under Section 6015(c)

Equitable Relief

IRC Section 6015(f)



- Only available if no relief is permitted under IRC Section 6015(b) or (c)
- Relief is available for amounts shown on the return, but which remain unpaid
- Refunds are available

Rev. Proc. 2013-34



- A requesting spouse must satisfy **ALL** of the following **threshold conditions** to be eligible to submit a request for equitable relief under IRC section 6015(f).
 - Joint return filed
 - Relief is not available under IRC sections 6015(b) or (c)
 - Timely Request
 - No assets were transferred between the spouses as part of a fraudulent scheme by the spouses

Rev. Proc. 2013-34



- The nonrequesting spouse did not transfer disqualified assets to the requesting spouse.
 - Not applicable if the requesting spouse was subject to abuse, or the non-requesting spouse had restricted access to financial information, or was unaware of the transfer
- The requesting spouse did not knowingly participate in the filing of a fraudulent joint return
- The income tax liability from which the requesting spouse seeks relief is attributable (either in full or in part) to an item of the nonrequesting spouse or an underpayment resulting from the nonrequesting spouse's income

Streamlined Determinations



- If the threshold conditions are met the IRS will consider granting equitable relief provided that the requesting spouse:
 - Is no longer married to the nonrequesting spouse.
 - Would suffer economic hardship if relief were not granted ; and
 - Did not know or have reason to know that there was an understatement or deficiency on the joint return, or did not know or have reason to know that the nonrequesting spouse would not or could not pay the underpayment of tax reported on the joint income tax return.
 - This condition does not need to be met if there was abuse by the nonrequesting spouse, or the nonrequesting spouse maintained control over the household finances by restricting access to the financial information

Non-Streamlined Determinations (Summary)

- Marital Status
- Economic Hardship
- Knowledge
- Abuse
- Legal Obligation
- Significant benefit
- Compliance with Income Tax Laws
- Mental or Physical Health

Non-Streamlined Determinations



- Facts and Circumstances. No factor is controlling. Factors are classified as favorable, unfavorable, or neutral.
 - Marital Status. If the parties are legally separated, divorced, widowed, or not part of the same household during the 12 month period ending on the date of the IRS determination. Favorable, or Neutral.
 - Economic Hardship. Favorable or Neutral
 - Lack of economic hardship is neutral (New)
 - Economic hardship means unable to pay basic living expenses. Treas. Reg. Section 301.6343-1(b)(4). However, the standards as applied by the Tax Court are more flexible than for offers in compromise. See e.g. [*Nihiser v. Comm'r, T.C. Memo 2008-135 \(T.C. 2008\)*](#)

Factors (Cont.)



- Knowledge. Generally Favorable or Unfavorable.
 - Knowledge is not a “super factor”
 - Understatement Cases
 - Did not know and had no reason to know of the understatement
 - Underpayment cases.
 - Whether the requesting spouse knew or had reason to know at the time the requesting spouse signed the joint return that the nonrequesting spouse would not or could not pay the tax liability at the time the joint return was filed or within a reasonably prompt time after the filing of the joint return.
 - if a request for an installment agreement to pay the tax was filed by the later of 90 days after the due date for payment, or 90 days after the return was filed then the spouse will be presumed not to know

Reason to Know Criteria Include



- Requesting spouse's level of education,
- Any deceit or evasiveness of the nonrequesting spouse,
- The requesting spouse's degree of involvement in the activity generating the income tax liability,
- The requesting spouse's involvement in business and household financial matters,
- The requesting spouse's business or financial expertise, and any lavish or unusual expenditures compared with past spending levels.

More Factors

- Abuse by the nonrequesting spouse. Favorable or neutral. Abuse can cause other factors to swing from unfavorable to favorable.
 - Contrast abuse v. duress
 - Abuse can be psychological or emotional as well as physical
 - Impact of the nonrequesting spouse's alcohol or drug abuse is considered
- Legal obligation. Favorable, unfavorable, or neutral.
 - This factor will weigh in favor of relief if the nonrequesting spouse has the sole legal obligation to pay the outstanding income tax liability pursuant to a divorce decree or agreement
 - Neutral if the requesting spouse knew or had reason to know, when entering into the divorce decree or agreement, that the nonrequesting spouse would not pay the income tax liability.
 - Against relief if the requesting spouse has the sole legal obligation.
 - If both spouses have a legal obligation to pay the outstanding income tax liability, the spouses are not separated or divorced, or the divorce decree or agreement is silent this factor is neutral.

Yet More Factors

- Significant benefit. Whether the requesting spouse received significant benefit (beyond normal support) from the unpaid income tax liability or item giving rise to the deficiency. Favorable or neutral.
- Compliance with income tax laws. Whether the requesting spouse has made a good faith effort to comply with the income tax laws in the taxable years following the taxable year or years to which the request for relief relates.
- Mental or physical health. Whether the requesting spouse was in poor physical or mental health.
 - This factor is always either positive, or neutral

Appealing an Adverse Decision

- IRS issues Notice of Preliminary Determination
- Filing a Protest with the Appeals Division-30 day time limit
- Filing a Tax Court Petition
 - After a Final Notice of Determination by the Appeals Division
 - After 6 months have elapsed since the filing of the initial request
 - Tax Court Petition may also be filed in connection with a substantive deficiency determination.
 - Failure to raise innocent spouse defense may permanently prevented from being raised if the spouse “meaningfully participated” in the Tax Court case.
- Tax Court Review
 - Scope of review is de novo and standard of review is de novo. *Wilson v. Commissioner*, 705 F.3d 980 (9th Cir. 2013), *acq.* AOD IRB 2013-25 (June 17, 2013).
 - The Court can therefore receive evidence not submitted to Appeals, AND the Court reviews the case without regard to the IRS’ determination.
- Innocent spouse defense may also be raised as part of a CDP hearing. IRC Section 6330(c)(2)(A).
- Innocent Spouse Reconsideration. See IRM 25.15.17
 - Includes a right to Appeals Consideration
 - But no right to go to Tax Court

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