

OFFICE OF TAX APPEALS
STATE OF CALIFORNIA

In the Matter of the Appeals of:) OTA Case Nos. 18011011, 18011341
)
B. PROCTOR AND)
)
J. NICOL)
)
_____)

OPINION

Representing the Parties:

For B. Proctor: Michael P. Setty, Esq.
For J. Nicol: Steven R. Williams, Esq.
For Respondent: Brian Werking, Tax Counsel
Michael J. Cornez, Tax Counsel V

For Office of Tax Appeals: William J. Stafford, Tax Counsel III

T. LEUNG, Administrative Law Judge: Pursuant to California Revenue and Taxation Code (R&TC) sections 18533 and 19045, B. Proctor (appellant-husband) and J. Nicol (appellant-wife) appeal from the actions of respondent Franchise Tax Board (FTB) for taxable years 1976 through 1979 (the taxable years at issue).¹

Appellants waived their right to an oral hearing and therefore these consolidated appeals are decided on the written record.

ISSUES

1. Whether appellants demonstrated error in FTB’s proposed assessments of additional tax, plus applicable interest, for the taxable years at issue, as revised by FTB during this appeal.
2. Whether appellant-wife is entitled to innocent spouse relief for the taxable years at issue.

¹ Appellant-husband and appellant-wife were formerly married and filed separate appeals—appellant-husband, Case No. 18011011, and appellant-wife, Case No. 18011341—in relation to FTB’s proposed assessments for the taxable years at issue. During the appeal proceedings, appellant-wife submitted a request for innocent spouse relief, which appellant-husband opposed. The age of the tax years at issue is primarily due to pending litigation regarding some of the federal adjustments, as discussed below.

FACTUAL FINDINGS

1. Appellants were married and filed joint returns for the taxable years at issue; their divorce was finalized in 1984.
2. FTB examined appellants' California personal income tax returns for the taxable years at issue and made several proposed adjustments, including the add-back of unreported income from the Westoaks Investment No. 17 partnership (Westoaks) for 1976 and disallowing interest expense deductions attributable to the Kersting tax shelters (Kersting Shelters) for each of the taxable years at issue.
3. In 1982, FTB issued notices of proposed assessment (NPAs) reflecting these audit adjustments.
4. Appellants protested the NPAs.
5. For the 1976 taxable year, appellants contested all FTB adjustments except for the adjustments related to partnership income of \$4,599 and partnership capital gains of \$1,029.
6. For the 1977 and 1979 taxable years, appellants contested all FTB adjustments.
7. For the 1978 taxable year, appellants asserted that FTB's adjustment of \$8,180 for partnership income should be reduced to \$1,470²—and they contested all of the remaining FTB adjustments.
8. During protest, FTB received information indicating that the Internal Revenue Service (IRS) had disallowed the same interest expense deductions related to the Kersting Shelters that FTB had disallowed, and that the deductibility of interest expenses involving the Kersting Shelters was being litigated in U.S. Tax Court; the U.S. Tax Court decision was appealed. Appellants requested the deferral of their protest pending a final resolution in the Kersting Shelters litigation.
9. In *Hongsermeier v. Commissioner* (9th Cir. 2010) 621 F.3d 890 (*Hongsermeier*), the Ninth Circuit held that (1) with respect to deductions related to the Kersting Shelters, the taxpayer would have 63.37 percent allowed, or stated another way, 36.63 percent of the claimed deductions would be disallowed; (2) all penalties, whether related to the Kersting

² FTB asserts that appellants provided some "information" supporting a finding that the adjustment of \$8,180 should be reduced to \$1,470; FTB subsequently conceded the remaining \$6,710 of the \$8,180 partnership income adjustment.

Shelters or otherwise, were eliminated; (3) all non-Kersting Shelter related penalties, additions, and deficiencies for all affected Kersting Shelter taxpayers were eliminated; and (4) interest was suspended on the Kersting Shelter adjustments from June 1992 until September 13, 2007.

10. Although FTB periodically followed up with appellants to determine the status of the IRS action, appellants never reported termination of the IRS matter to FTB. Ultimately, FTB received information from the IRS that the federal matter was completed, and in response, FTB issued Notices of Action (NOAs) dated May 30, 2017, affirming the NPAs for the taxable years at issue.
11. Appellant-husband and appellant-wife filed separate appeals from the NOAs, which Office of Tax Appeals (OTA) consolidated.
12. On appeal, FTB states that for each taxable year at issue, it will adjust the respective NPA, as set forth immediately below.
13. For the 1976 taxable year, appellants agreed with the adjustments related to partnership income of \$4,599 and partnership capital gains of \$1,029. FTB will reduce the two adjustments related to the Kersting Shelters from a combined total of \$16,084 to a combined total of \$5,892. Also, FTB will suspend interest owed on the revised Kersting Shelter adjustments totaling \$5,892 from June 1992 until September 13, 2007, in a manner similar to the approach taken in *Hongsermeier*. In addition, FTB states that an amnesty penalty will be applied to the non-Kersting Shelter adjustments.³ In summary, FTB's revised calculations on appeal of the amounts owed for the 1976 taxable year are as follows:

| | |
|--------------------------|-------------------|
| Additional Tax | \$1,104.18 |
| Interest through 4/30/19 | \$15,924.76 |
| Amnesty Penalty | <u>\$3,193.28</u> |
| Total | \$20,222.22 |

³ The jurisdiction of OTA to review an amnesty penalty is extremely limited. A taxpayer has no right to an administrative protest or appeal of an unpaid amnesty penalty. (R&TC, § 19777.5(d).) A taxpayer also has no right to file an administrative claim for refund of a paid amnesty penalty, except upon the basis that the penalty was not properly computed. (R&TC, § 19777.5(e).) Therefore, the OTA's jurisdiction to review an amnesty penalty is limited to situations where the penalty is assessed and paid, the taxpayer files a timely appeal from a denial of a refund claim, and the taxpayer attempts to show a computational error in the penalty. That situation is not present here. Accordingly, we will not further address the amnesty penalties.

14. For the 1977 taxable year, FTB will reduce the Kersting Shelter adjustments from a combined total of \$20,663 to a combined total of \$7,569. Also, FTB will suspend interest owed on the revised Kersting Shelter adjustments totaling \$7,569 from June 1992 until September 13, 2007, in a manner similar to the approach taken in *Hongsermeier*. In addition, FTB states that an amnesty penalty will be owed. In summary, FTB's revised calculations on appeal of the amounts owed for the 1977 taxable year are as follows:

| | |
|--------------------------|----------------|
| Additional Tax | \$849.92 |
| Interest through 4/30/19 | \$5,184.78 |
| Amnesty Penalty | <u>\$58.15</u> |
| Total | \$6,092.85 |

15. For the 1978 taxable year, FTB will reduce the Kersting Shelter adjustments from a combined total of \$34,270 to a combined total of \$12,553. Also, FTB will suspend interest owed on the revised Kersting Shelter adjustments totaling \$12,553 from June 1992 until September 13, 2007, in a manner similar to the approach taken in *Hongsermeier*. In addition, FTB will accept appellants' position that the \$8,180 adjustment for partnership income should be reduced to \$1,470. FTB also states that an amnesty penalty will be owed. In summary, FTB's revised calculations on appeal of the amounts owed for the 1978 taxable year are as follows:

| | |
|--------------------------|-----------------|
| Additional Tax | \$1,462.67 |
| Interest through 4/30/19 | \$10,260.20 |
| Amnesty Penalty | <u>\$832.12</u> |
| Total | \$12,554.99 |

16. For the 1979 taxable year, FTB will reduce the Kersting Shelter adjustments from a combined total of \$33,341 to a combined total of \$12,213. Also, FTB will suspend interest owed on the revised Kersting Shelter adjustments totaling \$12,213 from June 1992 until September 13, 2007, in a manner similar to the approach taken in *Hongsermeier*. In addition, FTB eliminated the contested \$10,000 assessment of income from the sale of a partnership interest unrelated to the Kersting Shelter. FTB also states that an amnesty penalty will be owed. In summary, FTB's revised calculations on appeal of the amounts owed for the 1979 taxable year are as follows:

| | |
|--------------------------|----------------|
| Additional Tax | \$1,308.09 |
| Interest through 4/30/19 | \$6,465.65 |
| Amnesty Penalty | <u>\$10.10</u> |
| Total | \$7,783.84 |

17. Appellants did not demonstrate error with FTB’s proposed assessments of additional tax, plus applicable interest, as revised.
18. In June 2017, appellant-wife filed a request for innocent spouse relief (FTB Form 705) for the taxable years at issue.
19. Appellant-wife has a high school diploma, was not involved in preparing the tax returns for the taxable years at issue, did not review the returns before signing them, did not know income was underreported on the returns, and was not aware of appellant-husband’s investment in a tax shelter.
20. In addition, appellant-wife indicated that for the taxable years at issue, she was aware that appellant-husband earned income as an airline pilot, they had no financial difficulties and made no large purchases. Further, appellant-wife stated that during the taxable years at issue, no assets were transferred to her. She also asserted that she has assets of only \$1,000. In addition, appellant-wife stated, in a general manner, that she was a victim of various forms of spousal abuse during the taxable years at issue, and in particular that appellant-husband had threatened her, her children, or members of her family; had made her afraid to disagree with him; had criticized or insulted her frequently; had made most of the family’s financial decisions; and had restricted or controlled who she could visit or talk with.
21. FTB issued a Non-Requesting Taxpayer Notice to appellant-husband, advising him of appellant-wife’s request for innocent spouse relief for the taxable years at issue and provided him with an opportunity to submit information and documentation.
22. Appellant-husband responded to FTB’s notice, asserting that FTB should deny appellant-wife’s request for innocent spouse relief and that the U.S. Tax Court had previously denied appellant-wife’s federal request for innocent spouse relief during the Kersting Shelters litigation.
23. FTB then sent a letter to appellants requesting information regarding their partnership interest in Westoaks.

24. In response, appellant-husband sent FTB a letter asserting that appellant-wife was involved in the decision to invest in Westoaks. Specifically, appellant-husband stated that they got involved with Westoaks through appellant-husband's cousin, O. Phillips. Elaborating further, appellant-husband stated that Mr. Phillips came to their house and the three of them (appellant-husband, appellant-wife, and Mr. Phillips) sat down at the kitchen table while Mr. Phillips "went over the pros" of investing in Westoaks. Appellant-husband asserted that both he and appellant-wife agreed to participate in Westoaks and that if there was any income from Westoaks, they would both receive the same benefit. In addition, appellant-husband asserted that appellant-wife received numerous other benefits (such as a new car in 1977 and various trips) from their other investments and income. With his letter, appellant-husband enclosed a copy of a 1977 Schedule K-1, which indicated that appellant-husband and appellant-wife held a partnership interest in Westoaks, that their partnership interest in Westoaks terminated during the 1977 taxable year, and that Westoaks reported a net loss of \$1,075 for that taxable year.⁴
25. Later, FTB received a declaration, signed under penalty of perjury, from appellant-wife in which she indicated that she was a stay-at-home mother with a high-school education, that she was prohibited from working outside the home by appellant-husband, that she was a signatory on a joint bank account used for household expenses, and that appellant-husband maintained financial accounts separate from the bank account used for the family's household expenses. Appellant-wife also indicated that all investment decisions were made by appellant-husband and that she was not aware of the Kersting Shelters investments and the investment in Westoaks until their divorce proceedings in 1984. Further, she stated, in a general manner, that appellant-husband was "secretive" regarding their finances. In addition, appellant-wife stated that she was not aware of any large purchases during the taxable years at issue. She acknowledged, however, that appellant-husband purchased a Beech Baron airplane during their marriage, the specific time of which she stated she could not recall.

⁴ As noted in a footnote above, the record contains a copy of a 1976 Schedule K-1 for Westoaks, which indicates that appellant-husband and appellant-wife were owners of a partnership interest in Westoaks for the 1976 taxable year.

26. FTB determined that for taxable years 1977, 1978, and 1979, appellant-wife is entitled to full traditional innocent spouse relief under R&TC section 18533(b), and that for taxable year 1976, appellant-wife is entitled to partial traditional innocent spouse relief under R&TC section 18533(b) except for her half of appellants' Westoaks partnership interest.

DISCUSSION

Issue 1: Whether appellants demonstrated error in FTB's proposed assessments of additional tax, plus applicable interest, for the taxable years at issue, as revised by FTB during this appeal.

Income tax deductions are a matter of legislative grace, and a taxpayer who claims a deduction has the burden of proving by competent evidence that he or she is entitled to that deduction. (See *New Colonial Ice Co. v. Helvering* (1934) 292 U.S. 435; *Appeal of Myers* (2001-SBE-001) 2001 WL 37126924.) Unsupported assertions are not sufficient to satisfy a taxpayer's burden of proof. (*Appeal of Magidow* (82-SBE-274) 1982 WL 11930.)

FTB's determinations are presumed correct, and appellant bears the burden of proving error. (*Appeal of Brockett* (86-SBE-109) 1986 WL 22731; *Todd v. McColgan* (1949) 89 Cal.App.2d 509.) In the absence of credible, competent, and relevant evidence showing that FTB's determinations are incorrect, they must be upheld. (*Appeal of Seltzer* (80-SBE-154) 1980 WL 5068.) Unsupported assertions are not sufficient to satisfy an appellant's burden of proof. (*Appeal of Magidow* (82-SBE-274) 1982 WL 11930.) A taxpayer must report federal changes to income or deductions to FTB within six months of the date the federal changes become final. (R&TC, § 18622(a).) A taxpayer shall either concede the accuracy of a federal determination or state wherein it is erroneous. (*Ibid.*) A proposed deficiency assessment that is based on a federal audit is presumptively correct and the taxpayer bears the burden of proving otherwise. (*Appeal of Brockett, supra.*)

Appellants were provided an opportunity to present evidence showing error with the federal adjustments or with FTB's NPAs for the taxable years at issue, as revised; however, neither appellant has argued or provided evidence demonstrating any such error. Nor have they argued or submitted evidence showing that the IRS modified or canceled the applicable federal adjustments. Accordingly, we find no error with FTB's proposed assessments, as revised by FTB during this appeal.

Issue 2: Whether appellant-wife is entitled to innocent spouse relief for the taxable years at issue.

When a joint return is filed by a married couple, each spouse is jointly and severally liable for the entire tax due for that taxable year. (R&TC, § 19006(b); Internal Revenue Code (IRC), § 6013(d)(3).) Federal and California law, however, provide that an individual who files a joint return may, in certain circumstances, be relieved of all or a portion of such joint and several liabilities. (R&TC, § 18533; IRC, § 6015.)

When a California statute is substantially identical to a federal statute (as is the case of the innocent spouse statutes, IRC section 6015 and R&TC section 18533), federal law interpreting the federal statute may be considered highly persuasive with regard to the California statute. (*Douglas v. State of California* (1942) 48 Cal.App.2d 835, 838; *Rihn v. Franchise Tax Bd.* (1955) 131 Cal.App.2d 356, 360.) Thus, federal authority is applied extensively in California innocent spouse cases. (See R&TC, § 18533(g)(2).) Federal Treasury regulations are applied in California innocent spouse cases to the extent that such regulations do not conflict with R&TC section 18533 or FTB's regulations. (*Ibid.*)

Generally, an individual claiming relief has the burden of establishing each statutory requirement by a preponderance of the evidence. (*Friedman v. Commissioner* (2d Cir. 1995) 53 F.3d 523; *Stevens v. Commissioner*, T.C. Memo. 1988-63.) Because the innocent spouse provisions are remedial in nature, they are construed and applied liberally in favor of the individual claiming their benefits. (*Friedman v. Commissioner, supra*, at pp. 528-529.) Unsupported assertions, however, are not sufficient to satisfy an individual's burden of proof. (See *Appeal of Magidow, supra.*)

There are four types of innocent spouse relief under R&TC section 18533: traditional relief under subdivision (b); a separate liability election under subdivision (c); equitable relief under subdivision (f); and conforming relief under subdivision (i) when federal innocent spouse relief has been granted. Also, R&TC section 19006(b) provides that a court may revise a joint tax liability in a divorce proceeding.

In relation to conforming relief under R&TC section 18533(i), we note that the record contains no evidence that the IRS or a federal court granted appellant-wife innocent spouse relief

for any of the taxable years at issue—and none of the parties has asserted otherwise.⁵ Thus, appellant-wife is not entitled to conforming relief under R&TC section 18533(i). As for court-ordered relief under R&TC section 19006(b), the record contains no evidence that a court ever revised either of the appellant's 1976 through 1979 joint tax liabilities in a divorce proceeding — and none of the parties has asserted otherwise. Thus, appellant-wife is not entitled to court-ordered relief under R&TC section 19006(b). Accordingly, throughout the remainder of our opinion we will focus on whether appellant-wife qualifies under R&TC section 18533 for traditional innocent spouse relief under subdivision (b), separate liability relief under subdivision (c), or equitable innocent spouse relief under subdivision (f).

Traditional Innocent Spouse Relief

R&TC section 18533(b)(1) allows relief with respect to an understatement of tax attributable to the erroneous items of the other individual filing the joint return when the requesting spouse meets the following requirements:

1. A joint return was filed for the taxable year in issue;
2. The return contains an understatement of tax attributable to an erroneous item of the other spouse;
3. The requesting spouse established that in signing the return, he or she did not know of, and had no reason to know of, the understatement;
4. Taking into account all facts and circumstances, it would be inequitable to hold the requesting spouse liable for the deficiency attributable to the understatement; and
5. The requesting spouse's claim for relief is timely.

The requirements of R&TC section 18533(b)(1) are stated in the conjunctive. Thus, if the requesting spouse fails to meet any one of them, he or she does not qualify for innocent spouse relief. (See *Alt v. Commissioner* (2002) 119 T.C. 306, 313, *affd.* (6th Cir. 2004) 101 Fed. Appx. 34.) In determining whether an individual is entitled to traditional relief under subdivision (b) of R&TC section 18533, the proper standard and scope of review is *de novo*. (See, e.g., *Porter v. Commissioner* (2009) 132 T.C. 203, 210; *Thomassen v. Commissioner*, T.C. Memo. 2011-88.)

⁵ In fact, appellant-husband asserts that the U.S. Tax Court denied appellant-wife's request for innocent spouse relief during the Kersting Shelter litigation. We note, however, that no documents provided as part of the record support a finding that the U.S. Tax Court ever addressed or determined whether appellant-wife was an innocent spouse for the taxable years at issue.

It is undisputed that appellants filed joint returns for the taxable years at issue. Accordingly, appellant-wife has satisfied the first requirement for traditional innocent spouse relief.

With regard to the second requirement, to determine whether an erroneous item is attributable to a nonrequesting spouse, a court looks not only to how ownership is nominally held between the spouses but also to each spouse's level of participation in the activity which gave rise to the erroneous item. (*Juell v. Commissioner*, T.C. Memo. 2007-219.) Generally, a requesting spouse who voluntarily agrees to enter into an investment and who actively participates in it is precluded from attributing the entire investment to the nonrequesting spouse. (*Ibid.*) However, if the requesting spouse is not an active participant, the requesting spouse may qualify for relief even though that spouse is named as a shareholder or partner. (*Ibid.*; *Varela v. Commissioner*, T.C. Memo. 2014-222.) For traditional innocent spouse relief under R&TC section 18533(b), an item must be solely attributable to the nonrequesting spouse.⁶

Here, the record establishes that FTB's adjustments, as revised on appeal, for the taxable years at issue are solely attributable to erroneous items of appellant-husband, except for the appellants' partnership interest in Westoaks, which affects only the adjustments for the 1976 taxable year. As for the investment in Westoaks, we find that appellants were both involved in the investment in Westoaks, as evidenced by appellant-husband's statements that (1) appellants got involved with Westoaks through appellant-husband's cousin (Mr. Phillips), (2) the three of them (appellants and Mr. Phillips) sat down at the kitchen table while Mr. Phillips "went over the pros" of an investment in Westoaks, and (3) both appellants agreed to participate in Westoaks. In addition, a 1976 Schedule K-1 for Westoaks indicates that both appellants were owners of a partnership interest in Westoaks. Based on the foregoing, we find that the increase in partnership income from Westoaks is attributable to both appellants. This finding alone makes traditional innocent spouse relief unavailable as to the increase in partnership income from Westoaks (or any portion thereof) because the item was not solely attributable to appellant-husband.

As for the third requirement, a requesting spouse has knowledge or reason to know of an understatement if a reasonably prudent person in his or her position at the time he or she signed

⁶ *Work v. Commissioner*, T.C. Memo. 2014-190 [for purposes of traditional innocent spouse relief, the attribution requirement was met for certain items that were "solely attributable" to nonrequesting spouse; for other items that were not "solely attributable" to nonrequesting spouse, the attribution requirement was not met]; see also *Deihl v. Commissioner*, T.C. Memo. 2012-176.

the return could be expected to know that the return contained an understatement. (*Wiener v. Commissioner*, T.C. Memo. 2008-230.) Key factors include, but are not limited to, his or her education level and involvement in the family's business and financial affairs; the presence of lavish or unusual expenditures as compared to the family's past income levels, income standards, and spending patterns; and the nonrequesting spouse's evasiveness and deceit concerning the couple's finances. (*Butler v. Commissioner* (2000) 114 T.C. 276, 291.) Further, Treasury Regulation section 1.6015-2(c) identifies six nonexclusive factors that are relevant to the inquiry, which may overlap with the factors set forth immediately above: the nature and relative amount of the erroneous item; the couple's financial situation; the requesting spouse's educational background and business experience; whether the requesting spouse participated in the activity that resulted in the erroneous item; whether the requesting spouse inquired about the item; and whether the erroneous item represented a departure from a recurring pattern reflected in prior returns. A requesting spouse has a duty of inquiry. (*Mora v. Commissioner* (2001) 117 T.C. 279, 289.) However, where abuse or financial control by the nonelecting spouse is shown, a basis may exist for allowing innocent spouse relief. (See *Kistner v. Commissioner* (11th Cir. 1994) 18 F.3d 1521, 1526; see also Rev. Proc. 2013-34, § 4.03(2)(c).)

The returns for the taxable years at issue are fairly complicated with numerous sources of investment income and losses. Appellant-wife asserts that she has a high school education, that she did not participate in major family financial decisions, and that she did not have access to the separate financial accounts of appellant-husband. Nevertheless, the statements made by appellant-husband in response to appellant-wife's request for innocent spouse relief, along with the Schedule K-1 issued by Westoaks for the 1976 taxable year, support a finding that appellant-wife was involved with the appellants' investment in Westoaks and that she knew or should have known of the income from Westoaks for the 1976 taxable year. Although appellant-wife contends that appellant-husband was abusive and controlled their finances, there is insufficient evidence in the record that an exception for abuse or financial control applies.

On the whole, given the evidence, appellant-wife has established that on the dates she signed the returns she did not know or have reason to know of the adjustments itemized in FTB's NPAs for the taxable years at issue, except for the adjustment related to her partnership interest in Westoaks, which affects only the 1976 taxable year.

With regard to the fourth requirement, it must be shown that taking into account all facts and circumstances, it would be inequitable to hold the requesting spouse liable for the deficiency attributable to the understatement. (*Jacobsen v. Commissioner*, T.C. Memo. 2018-115.)

The IRS has identified several nonexclusive factors it considers relevant to this inquiry, which are set forth in Treasury Regulation section 1.6015-2(d) and in guidance issued under IRC section 6015(f) in Revenue Procedure 2013-34—and those factors are similarly applicable to an equitable inquiry under IRC section 6015(b). (*Jacobsen v. Commissioner*, *supra*.) A court may consult the factors set forth in Revenue Procedure 2013-34 when reviewing the government’s denial of relief on equitable grounds but is not bound to follow them. (*Ibid*.) Treasury Regulation section 1.6015-2(d) identifies the relevant factors as (1) whether the requesting spouse significantly benefited, directly or indirectly, from the understatement; (2) whether the nonrequesting spouse has deserted the requesting spouse; (3) whether the spouses are divorced or separated; and (4) whether the requesting spouse received a benefit from the understatement on the joint return. (*Ibid*.)

In addition, the IRS has identified the following factors in Revenue Procedure 2013-34 section 4.03(2) as relevant: (1) the current marital status of the spouses, (2) whether the requesting spouse would suffer an economic hardship if relief were not granted, (3) whether the requesting spouse knew or had reason to know of the understatement, (4) whether either spouse has a legal obligation to pay the outstanding income tax liability, (5) whether the requesting spouse significantly benefited from the understatement, (6) whether the requesting spouse has made a good faith effort to comply with the income tax laws in the years following the years for which relief is sought, and (7) whether the requesting spouse was in poor mental or physical health at the time the joint return was filed. (*Jacobsen v. Commissioner*, *supra*.)

1. Marital Status

This factor will weigh in favor of relief if the requesting spouse is no longer married to the nonrequesting spouse. (Rev. Proc. 2013-34, § 4.03(2)(a).) Because appellant-husband and appellant-wife have been divorced since 1984, this factor favors relief.

2. Economic Hardship

An economic hardship exists if satisfaction of the tax liability in whole or in part will cause the requesting spouse to be unable to pay reasonable basic living expenses. This factor is

determined based on rules similar to those provided in Treasury Regulation section 301.6343-1(b)(4), taking into account the requesting spouse's current income, expenses, and assets. (Rev. Proc. 2013-34, § 4.03(2)(b).)

The taxing agency will compare the requesting spouse's income to the federal poverty guidelines for the requesting spouse's family size and will determine by how much, if at all, the requesting spouse's monthly income exceeds the spouse's reasonable basic monthly living expenses. (*Ibid.*) If the requesting spouse's income is below 250 percent of the federal poverty guidelines, or if the requesting spouse's monthly income exceeds the requesting spouse's reasonable monthly living expenses by \$300 or less, then this factor will weigh in favor of relief unless the requesting spouse has assets out of which the requesting spouse can make payments towards the tax liability and still adequately meet the requesting spouse's reasonable basic living expenses. (*Ibid.*) If the requesting spouse's income exceeds these standards, then the taxing agency will consider all facts and circumstances in determining whether the requesting spouse would suffer economic hardship if relief is not granted. (*Ibid.*)

Here, appellant-wife has not provided a schedule of her current assets, liabilities, income, and expenses (signed under penalty of perjury or otherwise), along with evidence (e.g., invoices, cancelled checks, credit card statements) supporting such amounts. As noted above, unsupported assertions are not sufficient to satisfy an individual's burden of proof. (See *Appeal of Magidow, supra.*) Without more information as to the exact amounts of appellant-wife's current assets, liabilities, income, and expenses, the factor of economic hardship is unclear. In short, appellant-wife has not demonstrated economic hardship. Accordingly, this factor is neutral.

3. Knowledge or Reason to Know

As we determined above, appellant-wife has established that on the dates she signed the returns she did not know or have reason to know of the understatements in relation to FTB's adjustments for the taxable years at issue, except for FTB's adjustment related to the partnership interest in Westoaks, which affects only the 1976 taxable year. Further, as discussed above, although appellant-wife contends that appellant-husband was abusive and controlling, there is insufficient evidence in the record that an exception for abuse or control applies in this appeal. Accordingly, this factor favors relief, except for the adjustment related to the partnership interest in Westoaks, which affects only the 1976 taxable year.

4. The Nonrequesting Spouse's Legal Obligation

This factor will weigh in favor of relief if the nonrequesting spouse has the sole legal obligation to pay the outstanding tax liability under a divorce decree or a separate agreement. (Rev. Proc. 2013-34, § 4.03(2)(d).) This factor will be neutral if the divorce decree or separate agreement is silent as to any obligation to pay the outstanding income tax liability. (*Ibid.*) Here, no divorce decree or separate agreement has been submitted establishing that the tax liabilities are the sole legal obligation of either spouse. Therefore, this factor is neutral.

5. Significant Benefit to the Requesting Spouse

This factor will weigh in favor of relief if the nonrequesting spouse significantly benefited from the understatement and the requesting spouse had little or no benefit or the nonrequesting spouse enjoyed the benefit to the requesting spouse's detriment. (Rev. Proc. 2013-34, § 4.03(2).) If the amount of understatement was small and did not provide a benefit to either spouse, Revenue Procedure 2013-34 states that this factor will be neutral. (Rev. Proc. 2013-34, § 4.03(2)(e).) However, the U.S. Tax Court has held that this factor weighs in favor of relief if the requesting spouse received little or no benefit. (*Hollimon v. Commissioner*, T.C. Memo. 2015-157; *Wang v. Commissioner*, T.C. Memo. 2014-206.) A significant benefit is any benefit in excess of normal support. (Rev. Proc. 2013-34, § 4.03(2)(e).) Here, there is no evidence in the record that the applicable understatement or deficiency amounts significantly benefited either spouse, or that appellant-wife received little or no benefit. Accordingly, this factor is neutral.

6. Compliance with Income Tax Laws

This factor asks whether the requesting spouse has made a good faith effort to comply with income tax laws in the taxable years following the taxable year or years to which the request for relief was made. (See Rev. Proc. 2013-34, § 4.03(2)(f).) Here, FTB states that appellant-wife has "typically filed her returns" and does not have a balance due for any taxable year. Based on FTB's statements, we find that this factor favors relief.

7. Mental or Physical Health

This factor weighs in favor of relief if the requesting spouse was in poor mental or physical health when the return to which the relief relates was filed or when the request for relief

was made. (Rev. Proc. 2013-34, § 4.03(2)(g).) Appellant-wife has not alleged or provided evidence showing that she was in poor physical or mental health when she signed the returns for the taxable years at issue or when she requested innocent spouse relief. This factor is neutral.

8. Conclusion—Equity Factors

Given the evidence in the appeal record, we find that it would be inequitable to hold appellant-wife liable for the proposed assessments for the taxable years at issue, except for the adjustment related to the partnership interest in Westoaks, which affects only the 1976 taxable year.

As for the fifth requirement, the requesting spouse must have filed a request for innocent spouse relief no later than two years after the date when FTB commenced collection activities with respect to the individual. (R&TC, § 18533(b)(1)(E).) Here, FTB has not commenced collection activities. Thus, appellant-wife's request for innocent spouse relief was timely.

In conclusion, based on the analysis above, appellant-wife is entitled to traditional innocent spouse relief under R&TC section 18533(b) for the taxable years at issue, except for the adjustment related to the partnership interest in Westoaks, which affects only the 1976 taxable year. Because appellant-wife is not entitled to traditional innocent spouse relief under R&TC section 18533(b) for the adjustment related to the partnership interest in Westoaks, we will consider whether she qualifies for innocent spouse relief for the 1976 Westoaks adjustments under either R&TC section 18533(c) or (f).

Separate Liability Relief

R&TC section 18533(c) provides for allocation of a tax liability between spouses as if they had filed separate returns reporting their respective items of income and deduction. Treasury Regulations provide guidance as to the allocation of specific items. “Erroneous items of income are allocated to the spouse who was the source of the income.” (Treas. Reg. § 1.6015-3(d)(2)(iii).) “In the absence of clear and convincing evidence supporting a different allocation,” an erroneous income item relating to jointly owned assets “is generally allocated 50% to each spouse” (*Ibid.*)

To be eligible for separate liability relief under R&TC section 18533(c), the requesting spouse must establish that (1) the spouses filed joint returns for the taxable years at issue, (2) at the time the request for innocent spouse relief was made, the spouses were legally separated or

divorced or had not been members of the same household at any time during the previous 12 months; and (3) the election for relief was made after a deficiency was asserted but no later than two years after FTB began collection activities. (R&TC, § 18533(c).)

Appellant-wife clearly meets the three requirements set forth above. Nevertheless, an election for separate liability relief under R&TC section 18533(c) is invalid if FTB demonstrates that appellant-wife had actual knowledge, at the time she signed the 1976 return, “of any item giving rise to a deficiency (or portion thereof)” that was allocable to appellant-husband.⁷ (R&TC, § 18533(c)(3)(C).) The burden is on FTB to prove actual knowledge of any item giving rise to a deficiency (or portion thereof) by a preponderance of the evidence. (Treas. Reg. § 1.6015-3(c)(2)(i); *McDaniel v. Commissioner*, T.C. Memo. 2009-137.) Actual knowledge, however, will not bar relief under R&TC section 18533(c) if the requesting spouse establishes that she or he signed the return under duress.⁸ (R&TC, § 18533(c)(3)(C).)

Here, the evidence in the appeal record supports a finding that appellant-wife is not entitled to separate liability relief for the 1976 partnership income of Westoaks because, as discussed above, we find that appellant-wife had actual knowledge of the 1976 partnership income of Westoaks. We note that under Treasury Regulation section 1.6015-3(c)(2)(iv), joint ownership is a factor supporting a determination of actual knowledge and that a requesting spouse who resides in a community property state at the time a return was signed will be considered to have had an ownership interest in an item when the requesting spouse’s name appears on the ownership documents. Here, appellant-wife’s name appears with appellant-husband’s name on the 1976 Schedule K-1 issued by Westoaks. While a Schedule K-1 is not an “ownership document,” this evidence, combined with appellant-wife’s involvement in making the decision to invest in Westoaks, disqualifies her from separate liability relief. Hence, we will next consider appellant-wife’s request for relief under R&TC section 18533(f).

⁷ An election under R&TC section 18533(c) is also invalid if FTB demonstrates that assets were transferred between the individuals who filed the joint return as part of a fraudulent scheme. (R&TC, § 18533(c)(3)(A)(ii).) FTB has not argued, and there is no evidence, that assets were transferred as part of a fraudulent scheme.

⁸ As discussed above, we find that appellant-wife’s general assertions of abuse and financial control have not been substantiated.

Equitable Innocent Spouse Relief

R&TC section 18533(f) provides that FTB may relieve a taxpayer from a tax liability if: (1) taking into account all the facts and circumstances, it is inequitable to hold the taxpayer liable for the unpaid tax or understatement; and (2) the taxpayer does not otherwise qualify for relief under subdivisions (b) or (c). Determinations as to equitable relief are reviewed de novo, and the requesting spouse bears the burden of showing that he or she is entitled to equitable relief. (See *Wilson v. Commissioner* (9th Cir. 2013) 705 F.3d 980; *Porter v. Commissioner, supra.*)

As indicated above, appellant-wife is not entitled to traditional or separate liability innocent spouse relief under R&TC section 18533(b) or (c) for the 1976 Westoaks adjustment(s). IRS Revenue Procedure 2013-34 sets forth a three-step process to be followed in evaluating requests for equitable innocent spouse relief under IRC section 6015(f): (1) section 4.01 lists seven threshold conditions which must be met; (2) section 4.02 lists circumstances in which the IRS will make a streamlined relief determination; and (3) section 4.03 sets forth nonexclusive factors that the IRS will consider in determining whether relief should be granted because it would be inequitable to hold a requesting spouse jointly and severally liable.

Threshold Conditions—Section 4.01

Section 4.01 of Revenue Procedure 2013-34 sets forth the following seven threshold conditions⁹ for a taxpayer requesting equitable relief under IRC section 6015(f) (and, thus, the same factors will apply to our consideration under R&TC section 18533(f)):

1. The requesting spouse filed a joint return for the taxable year for which relief is sought;
2. Relief is not available to the requesting spouse under traditional innocent spouse relief or separate allocation innocent spouse relief;
3. The requesting spouse applies for relief within the applicable statute of limitations for requesting equitable relief;
4. No assets were transferred between spouses as part of a fraudulent scheme by the spouses;
5. The nonrequesting spouse did not transfer disqualified assets to the requesting spouse;

⁹ Revenue Procedure 2013-34, section 4.01, and federal court cases indicate that if the requesting spouse cannot satisfy all of the seven threshold conditions, then his or her claim for equitable relief under IRC section 6015(f) must be denied. (See, e.g., *Reilly-Casey v. Commissioner*, T.C. Memo. 2013-292; *Stanwyck v. Commissioner*, T.C. Memo. 2012-180; *Franc v. Commissioner*, T.C. Memo. 2010-79; *O'Meara v. Commissioner*, T.C. Memo. 2009-71.)

6. The requesting spouse did not file the return with a fraudulent intent; and
7. The income tax liability from which the requesting spouse seeks relief is attributable (in full or in part) to an item of the nonrequesting spouse or an underpayment resulting from the nonrequesting spouse's income. If the liability is partially attributable to the requesting spouse, then relief can be considered only for the portion of the liability attributable to the nonrequesting spouse. (Rev. Proc. 2013-34, § 4.01(7).) However, relief can still be considered regardless of whether the understatement, deficiency, or underpayment is attributable (in full or in part) to the requesting spouse, if a specified exception applies.¹⁰

Appellant-wife clearly meets the first two threshold conditions. With respect to the third threshold condition, we note that section 4.01(3) of Revenue Procedure 2013-34 provides that equitable relief must generally be filed before the expiration of the 10-year federal statute of limitations for collection under IRC section 6502. However, under R&TC section 19255, FTB has a 20-year collection statute of limitations, which runs from the latest "due and payable liability," including collection and lien fees. Here, FTB has not instituted collection activities, and therefore, the third threshold requirement is met.

With respect to threshold conditions 4, 5, and 6, there is no evidence to suggest that any assets were transferred between appellants, or that fraud was involved.

In relation to the seventh threshold condition, we note that income tax liability from which the requesting spouse seeks relief can be attributable (in full or in part) to an item of the nonrequesting spouse or an underpayment resulting from the nonrequesting spouse's income.¹¹ Here, appellant-wife meets the seventh threshold condition with respect to the 1976 proposed assessment attributable to appellant-husband's interest in Westoaks; thus, we must next analyze whether appellant-wife is entitled to streamlined relief (section 4.02) or factor relief (section 4.03).

¹⁰ The exceptions include: attribution solely due to the operation of community property law, nominal ownership, misappropriation of funds, and abuse or fraud committed by the nonrequesting spouse. (Rev. Proc. 2013-34, § 4.01(7).) We find that none of the exceptions is applicable.

¹¹ In comparison, as discussed above, for traditional innocent spouse relief under R&TC section 18533(b), an item of income has to be solely attributable to the nonrequesting spouse. (See *Work v. Commissioner, supra*; *Deihl v. Commissioner, supra*.)

Streamlined Determination—Section 4.02

Section 4.02 of Revenue Procedure 2013-34 provides the following list of factors which, if met, permit a streamlined determination of equitable innocent spouse relief:

- (1) the requesting spouse is no longer married to the non-requesting spouse;
- (2) the requesting spouse would suffer economic hardship if relief were not granted; and
- (3) the requesting spouse did not know or have reason to know that there was an understatement on the return.

Economic Hardship

As discussed in our analysis of traditional innocent spouse relief above, appellant-wife has not provided a schedule of her current assets, liabilities, income, and expenses (signed under penalty of perjury or otherwise), along with evidence (e.g., invoices, cancelled checks, credit card statements) supporting such amounts. Without more information as to the exact amounts of appellant-wife's current assets, liabilities, income, and expenses, the factor of economic hardship cannot be satisfied. In short, appellant-wife has not demonstrated economic hardship. Accordingly, appellant-wife does not qualify under the streamlined procedures of section 4.02. Hence, we focus on the nonexclusive factors of section 4.03.

Section 4.03 Factors

If the threshold conditions of section 4.01 are satisfied and streamlined equitable innocent spouse relief of section 4.02 is unavailable, then section 4.03 provides a list of nonexclusive factors to be weighed in making a decision. We have already addressed those factors in our analysis of traditional innocent spouse relief above, and the analysis of each factor produces the same result. Here, we find that appellant-wife is not entitled to section 4.03 factor relief for the proposed 1976 assessment for the Westoaks partnership interest, either as to appellant-husband's one-half portion thereof or for appellant-wife's one-half portion.

HOLDINGS

1. Appellants have not demonstrated error with FTB’s proposed assessments of additional tax, plus applicable interest, for the taxable years at issue, as revised by FTB on appeal.
2. Appellant-wife is entitled to full innocent spouse relief in relation to the proposed assessments for the taxable years at issue, except for FTB’s proposed 1976 assessment related to appellants’ Westoaks partnership interest, either for appellant-husband’s portion thereof or for appellant-wife’s portion.

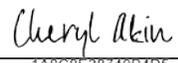
DISPOSITION

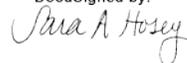
FTB’s NOAs, as revised and described herein above, are sustained; with respect to appellant-wife’s innocent spouse request, FTB’s action in granting same is sustained, except for the proposed 1976 assessment for the Westoaks partnership interest which is denied in full as described above.

DocuSigned by:

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 Tommy Leung
 Administrative Law Judge

We concur:

DocuSigned by:

 1A8C8E38740B4D5...
 Cheryl L. Akin
 Administrative Law Judge

DocuSigned by:

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 Sara A. Hosey
 Administrative Law Judge

Date Issued: 9/2/2020