

**OFFICE OF TAX APPEALS
STATE OF CALIFORNIA**

In the Matter of the Appeal of:) OTA Case No. 20025798
M. ALI (APPEALING SPOUSE) AND)
E. YOUNIS (REQUESTING SPOUSE))
_____)

OPINION

Representing the Parties:

For Appellant: Quirino Willie Jacques, CPA, MBA

For Respondent: Bradley J. Coutinho, Tax Counsel III

For Office of Tax Appeals: David Kowlczyk, Tax Counsel

S. HOSEY, Administrative Law Judge: Pursuant to Revenue and Taxation Code (R&TC) sections 18533 and 19045, M. Ali (appellant or non-requesting spouse) appeals an action by respondent Franchise Tax Board (FTB) granting innocent spouse relief to E. Younis (requesting spouse) for the 2011 and 2012 tax years.

Appellant waived the right to an oral hearing; therefore, the matter is being decided based on the written record.

ISSUE

Whether appellant has established that the requesting spouse does not qualify for innocent spouse relief for tax years 2011 and 2012.¹

¹ In addition, appellant initially argued that FTB issued the Notices of Proposed Assessment for tax years 2011 and 2012 after the expiration of the statute of limitations but withdrew this argument in his supplemental brief.

FACTUAL FINDINGS

Dubs Custom Tire Wheels and the Couple's Marriage

1. On November 5, 2005, the State Board of Equalization issued a Seller's Permit to appellant for Dubs Custom Tire Wheels (Dubs) and appellant began operating Dubs.²
2. In 2009, appellant and the requesting spouse (couple) were married in Pakistan.
3. In 2010, the requesting spouse arrived in the United States.
4. After the requesting spouse arrived in the United States, she could not sign Dubs' tax returns and did not have signature authority for Dubs' bank account.

Tax Return for Tax Years 2011 and 2012

5. On September 22, 2012, the couple filed a joint 2011 California Resident Income Tax Return. The couple provided their federal tax return showing they reported a Schedule C business called Dubs and appellant was the sole proprietor.
6. On April 8, 2013, the couple filed a joint 2012 California Resident Income Tax Return. However, the couple later filed an amended 2012 tax return and provided their federal tax return showing they reported a Schedule C business called Dubs and appellant was the sole proprietor.³

The Closing of Dubs and Divorce in Pakistan

7. On November 4, 2013, appellant filed a Statement of Abandonment of Use of Fictitious Business Name with the Fresno County Clerk for Dubs.
8. On December 11, 2013, the couple filed for divorce in Pakistan, which became effective on March 5, 2018.

Federal Adjustments for Tax Years 2011 and 2012

9. On August 10, 2015, FTB received information from the IRS showing that the IRS adjusted the couple's 2011 and 2012 federal tax returns.

² Appellant explained that he registered his name as the sole owner of Dubs because the couple was not married at the time when Dubs began.

³ The requesting spouse has consistently stated that she was not involved in the preparation of the couple's 2011 or 2012 tax returns and did not sign any documents.

FTB's Proposed Assessments for Tax Years 2011 and 2012 and Divorce in the United States

10. On June 2, 2016, FTB issued a Notice of Proposed Assessment (NPA) for tax years 2011 and 2012 based on the federal adjustments.
11. For tax year 2011, FTB proposed to assess \$31,287 of additional tax, plus interest. FTB proposed to disallow a \$23,567 expense for other business property, include \$362,493 of gross receipts for Dubs, and increase the self-employment tax deduction by \$9,702.
12. For tax year 2012, FTB proposed to assess \$37,550 of additional tax and impose a \$7,510 accuracy-related penalty, plus interest. FTB proposed to disallow a \$23,160 expense for other business property, disallow \$255,889 of costs of goods sold, include \$164,410 of gross receipts for Dubs, and increase the self-employment tax deduction by \$9,743.
13. On August 22, 2016, the NPAs for tax years 2011 and 2012 became final.
14. On October 19, 2017, the couple filed a petition for the dissolution of their marriage in California stating that they were separated on August 27, 2017.
15. On January 26, 2018, FTB began collection activity.

Requesting Spouse's Innocent Spouse Relief Request and Appeal

16. On February 12, 2019, the requesting spouse filed her Innocent Joint Filer Relief Request. The requesting spouse explained that she was separated from appellant on October 17, 2017, and the couple's divorce was pending.
17. On April 22, 2019, FTB issued a Request for Information to verify the requesting spouse's innocent spouse relief request. The requesting spouse explained that appellant filed the couple's tax returns in 2013 and she did not know how much income he earned.⁴ The requesting spouse explained that the couple only had one joint bank account with

⁴ The requesting spouse also explains that appellant transferred all of his property to his brother, which appellant disputes. However, this issue is not relevant to this appeal.

- Citibank that never had a balance exceeding \$3,000.⁵ The requesting spouse explained that appellant did not allow her to be a part of Dubs.⁶
18. On October 15, 2019, FTB issued a Non-Requesting Spouse Taxpayer Notice to appellant requesting appellant to provide more information about the requesting spouse's innocent spouse relief request. Appellant explained that they are both liable for the tax liability because the couple was married and operated Dubs together.
 19. On January 10, 2020, FTB issued a Notice of Action – Full Approval granting the requesting spouse's innocent spouse relief request.
 20. Thereafter, appellant timely filed this appeal.

FTB's Additional Documentation

21. On appeal, FTB requests more information from appellant and the requesting spouse. The requesting spouse reiterates that she was not involved in Dubs, did not review or sign the couple's tax returns, and had limited access to the couple's joint bank account.⁷
22. On June 20, 2020, appellant responds to FTB's request for information. Appellant reiterates that the requesting spouse was actively involved in Dubs and was responsible for maintaining Dubs' books and records, preparing sale and use tax returns, and customer service.⁸ Appellant explains that he merely reviewed the tax returns prepared by the requesting spouse and signed them. Appellant states he frequently signed whatever check or document the requesting spouse prepared for him. Appellant further

⁵ Appellant disputes this claim and provides a copy of the couple's Citibank statement showing they were joint owners. Appellant also provides a bank account statement showing that the bank account had a balance of \$10,473. However, every time the account balance was above \$10,000, the account balance would be reduced to below \$4,000 within approximately one week after the account balance was above \$10,000. Appellant denies knowledge of at least one of these transactions.

⁶ The requesting spouse also claims that she had full custody and appellant did not pay her child support, which appellant disputes. However, this issue is not relevant to this appeal.

⁷ The requesting spouse's statements may not be credible. The requesting spouse states that she had never been inside of Dubs. However, appellant provides several sworn statements from third parties stating that the requesting spouse took their orders. The requesting spouse later stated that she has been to Dubs to deliver lunch to appellant and his employees.

⁸ Appellant has also not been consistent about the requesting spouse's involvement with Dubs' bookkeeping. Initially, appellant stated that the requesting spouse merely kept the business records and delivered them to the bookkeeper, but he later stated that the requesting spouse prepared the sales and use tax returns and then provided that information to their bookkeeper who prepared the state income tax returns. Appellant then later stated that the requesting spouse "basically did the bookkeeping."

explains that the requesting spouse signed all of Dubs' invoices. Appellant provides a declaration from T. Fonesca stating that the requesting spouse took their orders and payments at Dubs. Appellant also provides invoices purportedly with the requesting spouse's signature.

23. On August 19, 2020, FTB issues a letter to appellant and the requesting spouse for more information.⁹
24. On September 16, 2020, appellant provides his response reiterating the same points that he has already made.
25. On October 16, 2020, the requesting spouse provides her response reiterating the same statements that she has already made. The requesting spouse also provides a copy of a police report, a letter from the Marjaree Mason Center, and a declaration from M. Walker describing events that she saw in March 2012 and May 2013.¹⁰
26. On February 10, 2021, the requesting spouse provides FTB a list of her income and expenses to determine whether she would suffer from economic hardship if she were held jointly liable for the couple's tax liability.
27. On February 14, 2021, I. Kaur, friend of requesting spouse, declares under penalty of perjury that the requesting spouse did not have any connection with Dubs and did not work at Dubs because she was pregnant with two children.¹¹

Appellant's Additional Documentation

28. After filing an appeal, appellant provides a declaration reiterating the same statements that he has already made. However, appellant provides several declarations from Dubs' customers stating that the requesting spouse took their orders and payments at Dubs.

⁹ FTB did not provide its August 19, 2020, letter, but appellant referred to the letter in its response to the letter.

¹⁰ The requesting spouse and FTB provided documentation establishing that the couple had an abusive relationship to negate the knowledge requirements in the innocent spouse statutes. However, it is not necessary to determine whether the requesting spouse established the domestic violence exception because the record does not establish that the requesting spouse had actual knowledge of Dubs' gross receipts and that Dubs did not incur its claimed expense for other business property and cost of goods sold.

¹¹ Appellant argues that I. Kaur did not have any actual knowledge of the requesting spouse's participation in Dubs because I. Kaur did not meet the requesting spouse until several years after Dubs closed in September 2013.

29. Appellant provides a sworn statement from R. Hauter declaring that he worked at Dubs for approximately four months beginning on September 1, 2012, while the requesting spouse was taking care of the couple's children.
30. Appellant provides declarations establishing his character, evidence of the requesting spouse's background, the couple's bank statements, the couple's utilities bills, several police reports, the couple's child custody and child support arrangement, the couple's living arrangements, and the couple's relationship.

DISCUSSION

Each spouse is jointly and severally liable for the tax on the aggregate income on the return when a joint return is filed. (R&TC, § 19006(b); Internal Revenue Code (IRC), § 6013(d).) However, an individual who files a joint return may be relieved of all or a portion of the joint and several liability if the individual qualifies for innocent spouse relief. (R&TC, § 18533(a); IRC, § 6015(a).) The three types of innocent spouse relief applicable in this appeal are traditional innocent spouse relief, separation of liability relief, and equitable relief. (R&TC, § 18533(b), (c), (f).) Innocent spouse determinations are made without regard to community property laws. (R&TC, § 18533(a)(2).)

The Treasury Regulations shall be applied to the extent that they do not conflict with California's innocent spouse statute or regulations. (R&TC, § 18533(g)(2).) Federal law interpreting a federal statute may be considered highly persuasive when interpreting a California statute that is substantially similar to a federal statute. (*Douglas v. State of California* (1942) 48 Cal.App.2d 835, 838.)

Determinations denying innocent spouse relief are reviewed *de novo*. (*Appeal of Pifer*, 2021-OTA-338P.) Generally, an individual claiming innocent spouse relief has the burden of establishing each statutory requirement by a preponderance of the evidence. (*Ibid.*) A taxpayer must provide uncontradicted, credible, competent, and relevant evidence to establish each statutory requirement. (*Ibid.*) Unsupported assertions are not sufficient to satisfy a taxpayer's burden of proof. (*Ibid.*)

I. Traditional Innocent Spouse Relief

The requesting spouse must satisfy all five requirements to be entitled to relief with respect to an understatement of tax:

- (1) A joint return was filed for a taxable year;
- (2) On that return there is an understatement of tax attributable to erroneous items of the requesting spouse filing the joint return;
- (3) The requesting spouse establishes 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 elects the benefits of this subdivision no later than the date that is two years after FTB has begun collection activities with respect to the individual making the election.

(R&TC, § 18533(b)(1)(A)-(E); IRC, § 6015(b); Treas. Reg. § 1.6015-2(a).)

An erroneous item is attributable to the individual whose activities gave rise to such item. (Treas. Reg. § 1.6015-1(f)(1).) The erroneous item must be solely attributable to the non-requesting spouse. (*Work v. Commissioner*, T.C. Memo. 2014-190.) Joint ownership alone does not dictate whether an erroneous item is allocated to one or both spouses. (*Juell v. Commissioner*, T.C. Memo. 2007-219.) The key factor is whether and to what extent the electing spouse voluntarily participated in the investment which gave rise to the erroneous item. (*Ibid.*) Generally, an electing spouse who voluntarily agrees to enter into an investment and who actively participates in it is precluded from attributing the entire investment to the nonelecting spouse. (*Ibid.*; *Varela v. Commissioner*, T.C. Memo. 2014-222.)

Here, the parties agree that the couple filed joint returns for tax years 2011 and 2012 and the requesting spouse timely requested innocent spouse relief. However, the parties dispute whether the erroneous items are attributable to appellant and/or the requesting spouse. The erroneous items that gave rise to the tax liability for tax years 2011 and 2012 are related to Dubs and appellant was the sole owner of Dubs. FTB argues that the requesting spouse did not participate at Dubs during tax years 2011 and 2012 and provides a third-party statement declaring that the requesting spouse did not participate at Dubs. Appellant argues that the requesting spouse actively participated at Dubs and was responsible for customer service and maintaining Dubs' books and records. Appellant provides several declarations from former Dubs' customers declaring that the requesting spouse took their orders and received their payments. The record contains credible statements from third parties contradicting the requesting spouse's assertion that she did not participate at Dubs. The requesting spouse's

burden, which was not met, is to provide uncontroverted evidence establishing that she did not actively participate at Dubs.¹²

Therefore, the requesting spouse has not established she is entitled to traditional innocent spouse relief for tax years 2011 and 2012.

II. Separate Allocation Relief

If an individual who has made a joint return for any taxable year elects for separation of liability relief, then the individual's liability for any deficiency that is assessed with respect to the return may not exceed the portion of the deficiency that is properly allocable to the individual. (R&TC, § 18533(c)(1).) To qualify for separation of liability relief, a requesting spouse must establish that: (1) he or she is no longer married to or is legally separated at the time the election is filed, (2) he or she made an election for separation of liability relief no later than two years after the date on which FTB has begun collection activities with respect to the individual making the election, (3) and the portion of any deficiency to allocate to the requesting spouse. (R&TC, § 18533(c)(2), (3)(A)(i)(I), (3)(B).)

Any item giving rise to a deficiency on a joint return shall be allocated to individuals filing the return in the same manner as it would have been allocated if the individuals had filed separate returns for the taxable year. (R&TC, § 18533(d)(3)(A).) Items of business income and expenses are allocated to the spouse who owned the business. (Treas. Reg. § 1.6015-3(d)(2)(iii), (iv).)

If FTB demonstrates that the requesting spouse had “actual knowledge” of the erroneous items that are allocable to the other spouse at the time the return was signed, then the election to allocate the deficiency attributable to those erroneous items are invalid and the requesting spouse remains liable for the portion of the deficiency attributable to those items. (R&TC, § 18533(c)(3)(C); Treas. Reg. § 1.6015-3(c)(2)(i).) However, actual knowledge may be established by a preponderance of the evidence as presented by all parties in cases where the non-requesting spouse intervenes to oppose FTB's granting innocent spouse relief. (*Knight v. Commissioner*, T.C. Memo. 2010-242; *McDaniel v. Commissioner*, T.C. Memo. 2009-137; *Stergois v. Commissioner*, T.C. Memo. 2009-15.) All the facts and circumstances are considered to determine whether the requesting spouse had actual knowledge. (Treas. Reg. § 1.6015-

¹² FTB acknowledges that the requesting spouse may have actively participated at Dubs based on the declarations provided by appellant.

3(c)(2)(iv).) We may also examine the surrounding facts and circumstances for an actual and clear awareness (as opposed to reason to know) of the existence of an item which gives rise to the deficiency. (*Cheshire v. Commissioner* (2000) 115 T.C. 183, 195; *Pounds v. Commissioner*, T.C. Memo. 2011-202.) This standard is not that of a hypothetical, reasonable person, but only that of the requesting spouse’s “actual subjective knowledge.” (*Culver v. Commissioner* (2001) 116 T.C. 189, 197; see also Treas. Reg. § 1.6015-3(c)(4), Examples 4 & 5.)

Here, the parties agree that the requesting spouse was no longer married to appellant at the time she filed her innocent spouse relief request, and the requesting spouse timely made an election for separation of allocation relief. The erroneous items for tax year 2011 are underreported gross receipts and the disallowed expenses for other business property for Dubs. The erroneous items for tax year 2012 are underreported gross receipts or sales, disallowed expenses for other business property, and disallowed cost of goods sold for Dubs. The record shows that appellant was the sole owner of Dubs and so the tax liability is solely allocable to appellant if the couple were to file separate tax returns. There is no evidence in the record to show that the requesting spouse actually knew any amount of Dubs’ gross receipts or that Dubs did not incur its claimed expenses for other business property and costs of goods sold.

Appellant argues that the tax liability should be allocable to the requesting spouse because she was Dubs’ co-owner. However, the couple’s tax returns list appellant as Dubs’ sole proprietor, the Seller’s Permit registered with the State Board of Equalization is registered to appellant, and the Statement of Abandonment of Use of Fictitious Business Name with the Fresno County Clerk for Dubs was signed by appellant. Appellant concedes that he began and operated Dubs for several years before he married the requesting spouse, who was still in Pakistan. There is also no evidence in the record to establish that the requesting spouse was able to assert any control over Dubs when appellant acknowledged that only appellant could sign Dubs’ tax returns and checks.¹³

Appellant argues that the requesting spouse had actual knowledge of Dubs’ income and expenses because the requesting spouse prepared Dubs’ books, records, and sales and use tax returns; collected money; prepared daily deposit slips; and ordered supplies and inventory.

¹³ Appellant argues that he is not able to provide additional evidence to support his assertions because the requesting spouse took Dubs’ records. To support this assertion, appellant provides a Fresno Police Report stating that a television, couches, and clothing were missing from the couple’s home. The police office called the requesting spouse who confirmed she took the children and the television, couches, and clothing because she believed appellant left her to go to Pakistan. However, the police report does not mention Dubs’ records.

However, appellant has not provided evidence to corroborate these assertions. While appellant provided evidence showing that the requesting spouse participated in Dubs by providing customer service and sales, there is no credible evidence in the record corroborating appellant's assertions that the requesting spouse actually knew any amount of Dubs' gross receipts or that the requesting spouse knew that Dubs did not incur its claimed expenses for other business property and costs of goods sold.

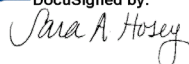
Therefore, the requesting spouse qualifies for separate allocation relief for tax years 2011 and 2012. We do not need to discuss whether the requesting spouse qualifies for equitable relief because the requesting spouse qualifies for separate allocation relief.

HOLDING

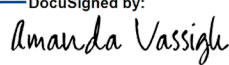
Appellant has not established that the requesting spouse does not qualify for innocent spouse relief for tax years 2011 and 2012.

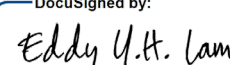
DISPOSITION

FTB's action in granting innocent spouse relief to the requesting spouse is modified to grant separate allocation relief under R&TC section 18533(c).

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 Sara A. Hosey
 Administrative Law Judge

We concur:

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 Amanda Vassigh
 Administrative Law Judge

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 Eddy Y. H. Lam
 Administrative Law Judge

Date Issued: 11/17/2022