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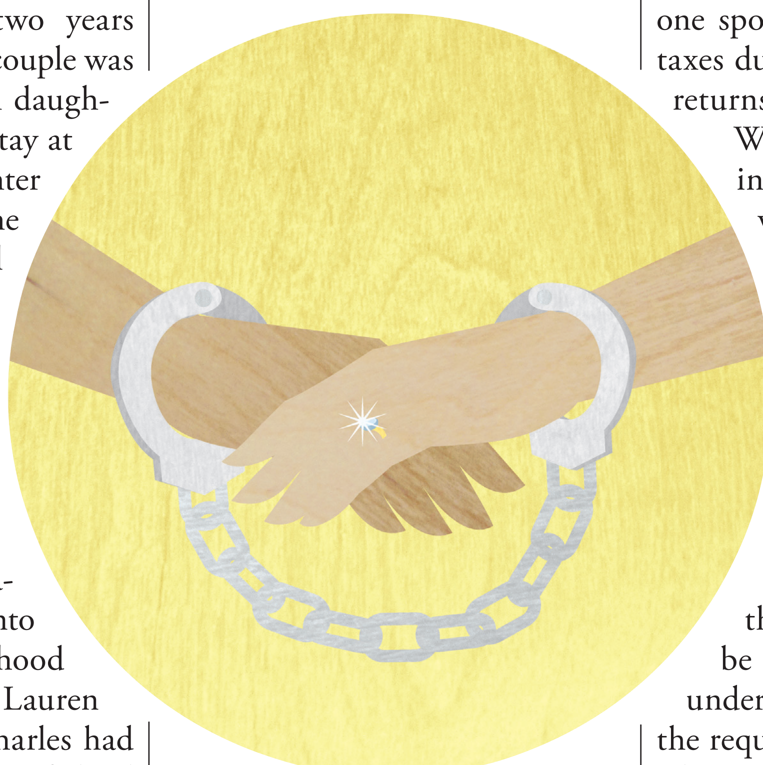
IS YOUR SPOUSE INNOCENT?

by MARIANNE MAN

Lauren thought she had married the perfect man. She and her husband, Charles, met at UCLA during their first year of college. He swept her off her feet with his intellect and charm, and when he received his acceptance into medical school at UCSF, she followed him. Charles proposed during his last year of his medical residency. Lauren felt her life was complete when, two years after they married, the couple was blessed with a beautiful daughter. Lauren decided to stay at home with her daughter and become a full-time homemaker. She left all financial decisions to her husband, whom she always knew to be trustworthy.

As Charles' medical practice grew in prosperity, Lauren's lifestyle grew more extravagant. They moved into an expensive neighborhood and bought exotic cars. Lauren never suspected that Charles had not only failed to pay their federal income taxes for the past five years, but that he had been cheating on her with his receptionist at his medical clinic. They filed their joint tax returns each year, and each time, Charles told her to sign the returns and insisted that she not waste her time reviewing the returns or the supporting documentation for the returns. Since Charles was a prominent doctor with a seemingly thriving medical practice, Lauren had no reason to suspect that Charles was not paying their tax obligations and was instead using the money to entertain his mistress. It was only after her daughter borrowed her father's iPad to play with, and



Lauren mistook the iPad for her own and opened the email application, that she discovered details of Charles' affair, as well as the financial problems with his medical practice, including Charles' failure to pay and taxes to the IRS and the California Franchise Tax Board.

Married taxpayers often choose to file a joint tax return. When filing a joint tax return, both spouses are responsible for the tax, and any interest or penalty due on the joint return even if they later divorce. Spouses remain jointly and severally liable even after one spouse dies, or even if a divorce decree provides that only one spouse is responsible for the taxes due on past jointly filed tax returns.

With those general rules in mind, whether Lauren would be jointly and severally liable in the above illustration depends on many factors. Some of the factors the IRS will consider include:

(1) Reasonable belief of the requesting spouse, at the time he or she signed the return, that the tax was going to be paid; or in the case of an understatement of tax, whether the requesting spouse had knowledge or reason to know of the understatement;

(2) Current financial hardship/inability to pay basic living expenses;

(3) Spouse's legal obligation to pay the tax liability pursuant to a divorce decree or agreement to pay the liability;

(4) To whom the liability is attributable;

(5) Significant benefit received by the requesting spouse;

(6) Mental or physical health of the requesting spouse on the date the requesting spouse signed the return or at the time the requesting spouse requested the relief;

(7) Compliance with income tax laws following the taxable year or years to which the request for relief relates; and

(8) Abuse experienced during the marriage.

There are three kinds of relief that many people collectively refer to as "innocent spouse relief." Many people confuse the requirements for the three different types of relief, especially since one of the three types of relief is named "innocent spouse relief." The other two types of relief are called "separation of liability" and "equitable relief," and together all three types are commonly referred to as "innocent spouse relief." Until relatively recently, a taxpayer must file a request for innocent spouse relief no later than two years after the first IRS attempt to collect the tax that occurs after July 22, 1998. On July 25, 2011, the IRS issued Notice 2011-70, which gave taxpayers more time to file for innocent spouse relief under the equitable relief theory. Equitable Relief Under Section 6015(f), I.R.S. Notice 2011-70, 2011-2 C.B. 135.

In order to obtain relief under the innocent spouse relief theory, one must meet all of the following conditions:

(1) The taxpayer must have filed a joint return, which has an understatement of tax;

(2) The understatement of tax must be due to erroneous items of the taxpayer's spouse;

(3) The taxpayer must establish that at the time that he or she signed the joint return, he or she did not know, and had no reason to know, that there was an understatement of tax;

(4) The IRS, after taking into account all of the facts and circumstances finds it would be unfair to hold the requesting taxpayer liable for the understatement of tax; and

Innocent spouse relief is one of the top most litigated issues by the IRS.

(5) The taxpayer must request relief within two years after the date on which the IRS first began collection activity against the taxpayer after July 22, 1998.

In order to meet the requirements under the separation of liability type of relief, the taxpayer must have filed a joint return and meet either of the following requirements at the time the request for such relief is made:

(1) The taxpayer is no longer married to, or is legally separated from, the spouse with whom the taxpayer filed the joint return for which the taxpayer is requesting relief from; or

(2) The taxpayer was not a member of the same household as the spouse with whom the taxpayer filed the joint return at any time during the twelve-month period ending on the date the taxpayer filed a request for relief.

The equitable relief option is only available if the innocent spouse relief and the separation of liability relief are not available to the taxpayer, and the IRS determines that it is unfair to hold the taxpayer liable for the understatement of tax after taking into the account all the facts and circumstances. The courts have not yet developed consistent interpretations of the law in this specific area; therefore, the IRS will base its decision upon all of the supporting information provided in each case.

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