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# HOW TO ADVISE YOUR CLIENTS ABOUT INNOCENT SPOUSE RELIEF AND BE THE HERO





## YOU WILL DISCOVER

- 1) How to save Your Clients from Unfair IRS Bills
- 2) The Risk of filing as Married-Filing-Joint
- 3) The Four Kinds of Relief and which of Your Clients may Qualify
- 4) Who may qualify as an Injured Spouse
- 5) How to Get Your Clients Help Now



# DAVID & DIANE




- ▷ David worked at an architectural firm
- ▷ Embezzled \$2 Million for Gambling Habit
- ▷ Diane works at a construction company
- ▷ They have two young children

\* Hypothetical based on Example in Treas. Reg. § 1.6015-2(e).

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David and Diane were married for ten years and have two young children. David worked at an architectural firm and Diane works for a large construction company. Two years ago, David was convicted of embezzling \$2 million from his employer. Diane did not find out about this until David was arrested. She also found out that David had used most of the funds to support his gambling habit. David put the funds in a separate account and transferred \$10,000 each month to their joint checking account from which Diane paid their household expenses. None of the \$2 million was included on their federal tax returns. They separated, and after a few months, Diane filed for divorce. The divorce was final last year. Diane has just received a notice from the Internal Revenue Service stating that two of their joint income tax returns are under audit.

Based on example in Treas. Reg. § 1.6015-2(e).



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## JOINT AND SEVERAL LIABILITY

- 1) General rule – spouses are jointly and severally liable for any tax due for any year they file a joint return
- 2) Marital status is determined as of the last day of the year
- 3) If spouses file separate tax returns, can amend within three years
- 4) If spouses file a joint return, must amend before the due date of the joint return





## INNOCENT SPOUSE RELIEF

- 1) Generally, two spouses who file a joint tax return are **jointly and severally liable** per I.R.C. section 6013(d)(3).
- 2) **Innocent Spouse Relief** is relief from joint and several liability for taxes owed by two spouses.
- 3) The **Requesting Spouse** is the spouse who requests relief.
- 4) Other spouse is the **Nonrequesting Spouse**.





# INNOCENT SPOUSE RELIEF

## Kinds of Innocent Spouse Relief:

- 1) § 6015(b) – erroneous item of one spouse
- 2) § 6015(c) – allocation of liability
- 3) § 6015(f) – equitable relief
- 4) § 66(c) – community property income





## INNOCENT SPOUSE RELIEF

### Requirements - I.R.C. § 6015(b) Relief – Erroneous Item

- 1) File joint tax return
- 2) Understatement attributable to erroneous item of one spouse
- 3) Other spouse did not know, or have reason to know, of understatement
- 4) Inequitable to hold liable for the tax
- 5) Elect within 2 years of IRS collection







# INNOCENT SPOUSE RELIEF

## Requirements - I.R.C. § 6015(b) Relief

- 1) File joint tax return
  - ▶ Signed by both spouses
  - ▶ Tacit Consent doctrine:

May be a valid return if spouses have a history of filing jointly with one spouse signing for both spouses





## INNOCENT SPOUSE RELIEF

### Requirements - I.R.C. § 6015(b) Relief

- 2) Understatement attributable to erroneous item of one spouse
  - ▶ Generally due to an IRS audit
  - ▶ The understatement is the difference between the tax reported and the tax that should have been shown
  - ▶ Erroneous Item – unreported income or illegitimate deduction or credit





## INNOCENT SPOUSE RELIEF

### Requirements - I.R.C. § 6015(b) Relief

- 3) Other spouse did not know, or have reason to know, of understatement – depends on:
  - ▶ Spouse's level of education
  - ▶ Involvement in business & finances
  - ▶ Standard of living – substantial increase
  - ▶ Nonrequesting spouse's evasiveness about family's finances





# INNOCENT SPOUSE RELIEF

## Requirements - I.R.C. § 6015(b) Relief

- 3) Other spouse did not know, or have reason to know, of understatement – Scenarios:
  - ▶ Withdrawal from an IRA
  - ▶ Income from exercise of stock options
  - ▶ Bonuses
  - ▶ Embezzled income





# INNOCENT SPOUSE RELIEF

## Requirements - I.R.C. § 6015(b) Relief

- 3) Other spouse did not know, or have reason to know, of understatement

### Santa v. Commissioner

- ▶ Mrs. Santa withdrew \$95k from profit-sharing account into joint account
- ▶ Mr. Santa used separate account, had no knowledge or benefit from income
- ▶ Tax Court granted Mr. Santa relief





# INNOCENT SPOUSE RELIEF

## Requirements - I.R.C. § 6015(b) Relief

- 3) Other spouse did not know, or have reason to know, of understatement

### Price v. Commissioner

- ▶ \$90,000 mining expenses deduction
- ▶ Reason to Know factors
- ▶ Constructive Knowledge – Duty of Inquiry





## INNOCENT SPOUSE RELIEF

### Requirements - I.R.C. § 6015(c) Relief - Allocation

- 1) File joint tax return
- 2) Understatement of tax
- 3) No longer married, legally separated, or not member of same household for 12 months
- 4) Elect within two years after start of IRS collection activities





# INNOCENT SPOUSE RELIEF

## Requirements - I.R.C. § 6015(c) Relief

### Collection Activities are:

- 1) A refund offset
- 2) Collection Due Process levy notice
- 3) The filing of a lawsuit by the U.S. to collect the joint liability, and
- 4) The filing of a claim by the IRS in a court proceeding.







## INNOCENT SPOUSE RELIEF

### Requirements - I.R.C. § 6015(c) Relief

A spouse is not eligible if:

- 1) assets are transferred between spouses as part of a fraudulent scheme, or
- 2) the spouse had actual knowledge when signing the tax return of any item giving rise to a deficiency.





# INNOCENT SPOUSE RELIEF

## Requirements - I.R.C. § 6015(c) Relief

Actual Knowledge:

### 1) Gonce v. Commissioner, T.C. Memo. 2007-327.

- ▶ Did not report income from Husband and Wife's paper routes in 1998-1999
- ▶ Husband only had routes after 1999
- ▶ Wife had actual knowledge of payments & could review returns





## INNOCENT SPOUSE RELIEF

### Requirements - I.R.C. § 6015(c) Relief

Actual knowledge defense:

- 1) Commissioner has burden of proof to show actual knowledge of the unreported income or erroneous deduction at the time the return was signed per I.R.C. section 6015(c)(3)(C).
- 2) IRS must allege facts in its answer in court to establish actual knowledge.





# INNOCENT SPOUSE RELIEF

## Requirements - I.R.C. § 6015(c) Relief

Actual knowledge defense

3) Erroneous deduction –

- ▶ Commissioner must show actual knowledge of the **factual circumstances** making the item unallowable as a deduction





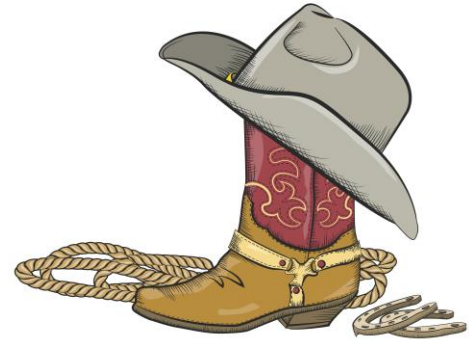
## INNOCENT SPOUSE RELIEF

### Requirements - I.R.C. § 6015(c) Relief

Actual knowledge defense

#### 3) Erroneous deduction –

- ▶ Tax Shelter cases
- ▶ Investors deceived about underlying facts – phantom cattle
- ▶ Spouse may or may not qualify for relief depending on level of knowledge of tax returns and finances





# INNOCENT SPOUSE RELIEF

## I.R.C. § 6015(c) Relief

- ▶ If granted, allocate liability between spouses per I.R.C. section 6015(d)
- ▶ Allocate erroneous items as if spouses had filed separate returns for the taxable year
- ▶ Allocate tax benefit items to the spouse who benefited





# INNOCENT SPOUSE RELIEF

## **Equitable Relief - I.R.C. § 6015(f)**

Governed by Revenue Procedure 2013-34

### **Threshold Eligibility Requirements - § 4.01**

- 1) File joint return
- 2) Relief n/a under I.R.C. § 6015(b), (c) (can be an underpayment)
- 3) Claim filed timely (by CSED date)
- 4) No assets transferred between spouses as part of a fraudulent scheme





# INNOCENT SPOUSE RELIEF

## **Equitable Relief - I.R.C. § 6015(f)**

Governed by Revenue Procedure 2013-34

### **Threshold Eligibility Requirements - § 4.01**

- 5) The nonrequesting spouse did not transfer disqualified assets to the requesting spouse
- 6) The requesting spouse did not knowingly participate in filing a fraudulent joint tax return, and







# INNOCENT SPOUSE RELIEF

## Equitable Relief - I.R.C. § 6015(f)

### Threshold Eligibility Requirements - § 4.01

- 7) The tax liability is attributable to an item of the nonrequesting spouse, unless:
  - ▶ solely due to community property law,
  - ▶ nominal ownership,
  - ▶ did not know of misappropriation of funds,
  - ▶ abused and feared retaliation if questioned, or
  - ▶ nonrequesting spouse's fraud caused liability.





# INNOCENT SPOUSE RELIEF

## Equitable Relief - I.R.C. § 6015(f)

### When to File Claim

- 1) Governed by new Rev. Proc. 2013-34
- 2) No requirement to elect within 2 years of IRS collection activity
- 3) File before expiration of the period of limitation for collection under section 6502, or the period of limitation for credit or refund under section 6511





# INNOCENT SPOUSE RELIEF

## Equitable Relief - I.R.C. § 6015(f)

### Streamlined Determinations

- 1) No longer married
  - ▶ Divorced, Legally Separated, Widow(er), Not in same household
- 2) Would suffer economic hardship if relief were not granted; and
- 3) Did not know or have reason to know of understatement/potential underpayment
  - ▶ Unless there is abuse or exclusive control of finances





# INNOCENT SPOUSE RELIEF

## Equitable Relief - I.R.C. § 6015(f)

### Equitable Factors:

- 1) Marital Status
- 2) Economic hardship
- 3) Knowledge/reason to know of item giving rise to the deficiency or understatement or of future nonpayment
- 4) Legal obligation to pay tax liability





## INNOCENT SPOUSE RELIEF

### Equitable Relief - I.R.C. § 6015(f)

#### Equitable Factors:

- 5) Significant Benefit
- Marzullo v. Commissioner,**  
**T.C. Memo. 2013-120**
- ▶ Pharmacist with own drug store
  - ▶ Mrs. Marzullo inherited store with \$1.3M life insurance proceeds
  - ▶ No relief because used tax funds to pay business expenses & insurance



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# INNOCENT SPOUSE RELIEF

## Equitable Relief - I.R.C. § 6015(f)

### Equitable Factors:

- 6) Compliance with tax laws in later years
- 7) In poor mental/physical health when sign



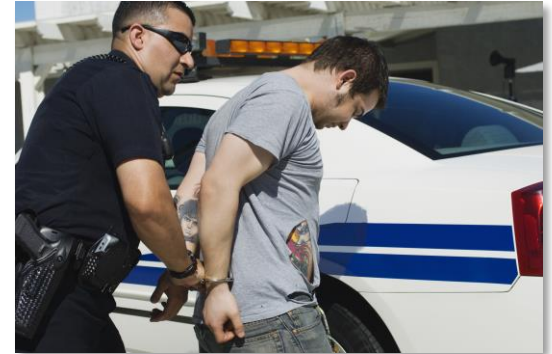


# INNOCENT SPOUSE RELIEF

## Equitable Relief - I.R.C. § 6015(f)

### Equitable Factors:

- 8) Abuse
  - ▶ Not a separate factor
  - ▶ Knowledge factor – favor relief  
Significant benefit factor – neutral
  - ▶ It is physical or psychological abuse so that spouse unable to question return or that taxes were paid for fear of retaliation





# INNOCENT SPOUSE RELIEF

## Equitable Relief - I.R.C. § 6015(f)

### Equitable Factors:

- 8) Abuse – Thomassen v. Commissioner, T.C. Memo. 2011-88.
  - ▶ IRS audit found inflated expenses
  - ▶ Tax Court found Mrs. Thomassen knew about understatements of tax
  - ▶ Entitled to equitable relief due to extreme psychological abuse







# INNOCENT SPOUSE RELIEF

## Equitable Relief - I.R.C. § 6015(f)

### Equitable Factors:

- 8) Abuse – Proof
  - ▷ Documentation: police reports, doctor's reports, restraining order
  - ▷ Specific allegations corroborated by third parties
  - ▷ Divorce pleadings



# \$ COMMUNITY PROPERTY INCOME

## I.R.C. § 66(c)

- 1) No joint return filed in a community property state
- 2) One spouse did not include on own separate return an item of community property income attributable to the other spouse
- 3) Spouse did not know of item of community property income
- 4) Inequitable for the spouse to pay tax on this income



# \$ COMMUNITY PROPERTY INCOME

## I.R.C. § 66(c)

### Hiramanek v. Commissioner, T.C. Memo. 2011-280

- 1) Joint return held invalid as signed under duress
- 2) Tax Court granted equitable relief under I.R.C. section 66(c) – divorced, economic hardship, did not benefit
- 3) Not have to include one-half share of ex-husband's wages in her income



## **\$ HOW TO REQUEST INNOCENT SPOUSE RELIEF**

### **File Form 8857, Request for Innocent Spouse Relief, with IRS.**

- 1)** Raise innocent spouse as a defense to a notice of deficiency in Tax Court
- 2)** Raise it as a defense in response to IRS collection action
- 3)** Within two years of IRS collection action if seeking I.R.C. section 6015(b) or (c) relief



## \$ HOW TO REQUEST INNOCENT SPOUSE RELIEF

### **File Form 8857, Request for Innocent Spouse Relief, with IRS.**

- 4) Can be found at:  
<https://www.irs.gov/pub/irs-pdf/f8857.pdf>
- 5) Part III – facts IRS looking for to show lack of knowledge, degree of involvement with household finances and significant benefit
- 6) Part IV – financial information for economic hardship determination



## \$ INJURED SPOUSE RELIEF

### Requirements:

- 1) Filed joint tax return
- 2) Entitled to a refund
- 3) Made tax payments or claimed refundable tax credit
- 4) IRS used refund to pay one spouse's legally-enforceable past-due debt
- 5) Spouse requesting relief not legally obligated to pay this past-due debt

If granted, spouse can be refunded their share of the overpayment.

**File Form 8379, Injured Spouse Allocation**



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# INNOCENT SPOUSE RELIEF

## Summary:

- 1) The kinds of innocent spouse relief available
  - ▶ I.R.C. § 6015(b) – erroneous item of one spouse
  - ▶ I.R.C. § 6015(c) – allocation of liability
  - ▶ I.R.C. § 6015(f) – equitable relief
  - ▶ I.R.C. § 66(c) – community property income
- 2) How to Request Relief from Joint and Several Liability



# DAVID & DIANE



- ▶ Relief for Diane under I.R.C. section 6015
- ▶ Relief for Diane under I.R.C. section 66(c) from tax on community property income







# COMPLIMENTARY CONSULTATION

## 20-minute consultation with Attorney Bob Boeshaar

- ▶ Discuss client's tax problems and potential solutions
- ▶ Find out if Your Client Might Qualify for Innocent Spouse Relief
- ▶ Contact us by phone or email or sign up yourself at <https://boeshaar.checkappointments.com/>.



# Questions about Innocent Spouse Relief?



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