Relief from Joint Liability on Joint Income Tax Returns

By Thomas R. White, III

Thomas R. White, III, in the first of a two-part article, analyzes the history and current state of innocent spouse law and explores the IRS’s recently issued guidance in this area.

When husband and wife sign a joint income tax return, they are jointly and severally liable for all tax liabilities associated with that return, including subsequently determined deficiencies. Joint and several liability preceded the enactment of income splitting, and, while not fully discussed in any of the earlier legislative histories, seems to have been predicated on collection issues. The changing demographics of the 1960s and later years soon made clear that imposition of joint and several liability in all cases would not be appropriate, and that relief from joint liability should be provided for some taxpayers.

The original “innocent spouse” relief provision stemmed from an unusual case in which the husband had embezzled from his wife’s business; his booty was held to be taxable income, includible on their joint return. Since only the wife had the resources to pay the tax, it was asserted against her on the basis of joint and several liability. She was clearly “innocent” in the colloquial meaning of the word, and so legislative relief was carefully framed to excuse only a spouse in her situation.

In the 1970s, the tax shelter industry reached maturity. These arrangements were designed to create deductible “losses” which would be used to reduce income from other sources. Since marginal rates were high, tax shelters were attractive. It was often the case that tax shelter investing was decided by only one of the spouses, again almost always the spouse with the higher income. The deductions claimed in many of these arrangements were later proved to be improper. As the Commissioner’s efforts to restrict the tax advantages began to bear fruit, instances of taxpayers against whom large liabilities were asserted because of tax shelter investments made by their spouses began to appear. While it was difficult to make the same “innocence” argument on behalf of many of these taxpayers, who were joint owners of the “investments” made by their spouses, there were frequent sympathetic cases in which the taxpayers were trapped in a situation over which they had no ap-

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parent control. Again, the Congress responded by enlarging the scope of innocent spouse relief to encompass deduction cases. The innocent spouse amendment, however, was drafted restrictively, to limit relief to "meritorious" cases. The basic requirements, the knowledge and equity rules, were retained, but for deduction cases, the statute required that the deduction of the item in question had to be "grossly erroneous," that is, tantamount to fraud.

The new provision immediately attracted the fire of the commentators. By this time, efforts to administer the innocent spouse relief provision had already shown how difficult relief was to obtain, even in situations where relief seemed appropriate. Most of the cases involved divorced taxpayers, facing liabilities created by inappropriate tax reporting for which an absent spouse had been completely responsible. The history of this provision in the courts has been thoroughly documented. It shows that reasonably competent taxpayers, even though completely ignorant of the tax effect of transactions done by their spouses, found obtaining relief next to impossible. Indeed, these cases produced dramatically inconsistent results on indistinguishable facts. The basic problem with the old rule was the lack of any administrable standard which can inform taxpayers as to how to protect themselves and courts as to the proper scope of relief.

These problems were well known by the early 1990s, but, for the same reasons that applicants found relief difficult to obtain, better administrative handling of innocent spouse claims seemed beyond reach. In this context, the Domestic Relations Committee of the ABA Tax Section undertook a careful study of joint and several liability for the purpose of determining whether a better defined relief provision could be developed. After much debate, the committee turned its work product into a report in which the committee recommended that spouses be authorized to elect to "separate their liabilities" on a joint return. It reached this result after concluding that revision of the original innocent spouse rule could not produce an appropriate result, because "innocence," at least in a tax sense, could never be an effective operating standard. The policy norm supporting the committee's work is that one taxpayer should not be liable for tax on another taxpayer's income. As a general rule in enforcement of an individual income tax, this norm is hardly debatable, but in the context of marital property rules and joint reporting, it fails to take account of the real complexity in the interaction between tax collector and the individual taxpayer.

The committee's recommendation made its way through the Tax Section and thence to the ABA House of Delegates, where it was passed in February 1995. Because this recommendation played an important role in the enactment of the spousal relief provisions of the IRS Restructuring and Reform Act ("1998 Act"), it is necessary to say a few things about it. The Domestic Relations Committee shaped its recommendation to deal with two separate problems. The first, subsequent imposition of tax deficiencies on one spouse for incorrect or fraudulent tax reporting by the other, is the classic situation for which the innocent spouse rule was designed. In the committee's view, neither spouse should be relieved of liability for that spouse's own share of tax on the joint return, but neither should a taxpayer be compelled to pay his or her spouse's share. At first, therefore, the Committee proposed a "proportional" liability standard which would have required determining each spouse's proper share of tax, taking the deficiency into account, and the portion he or she had actually paid. The recommendation would have precluded refunds of payments with respect to the tax reported on the return, in the ABA approval process, the committee simplified its approach by turning to the idea that joint filers should be able to separate their liabilities for deficiencies. The second problem involves failure to pay tax shown to be due on a joint return filed by the taxpayer and his or her spouse. Tax reported on a return is an assessed tax. The innocent spouse rule provided relief from deficiencies in tax, not from failure to pay an assessed tax. This issue was reported in cases brought through low income taxpayer clinics where the taxpayer's spouse had been entrusted with (or had access to) the funds necessary to pay the tax but had failed to do so. The taxpayer was not aware that the tax had not been paid until the IRS began collection activity.

The committee's original proportional liability standard worked neatly for both of these problems. It permitted the actual payments made by one spouse to be taken into account in determining later respon-
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Sibility for payment of tax no matter what the source of the liability might be. When the committee's proposal was shifted to a separation of liability approach for deficiencies, the committee retained the proportional liability rule for nonpayment cases.

Innocent spouse relief is now, as it was originally, a collection issue.

Its recommendation, therefore, had two distinct approaches to the problem, and this has sometimes led to confusion about the actual recommendation.

While the ABA was adopting the Domestic Relations Committee's legislative recommendation, spousal liability for tax on joint returns was becoming a much livelier topic. The Ways and Means Committee had raised concerns about it in its consideration of legislation that became the Taxpayer Bill of Rights II ("TBOR 2"). In early 1996, the Treasury announced its study of joint and several liability. The ABA proposal was one of several proposals analyzed in that report, while the Senate was considering the 1998 Act. In this report, the Treasury adhered to its earlier position, opposing the separation of liability idea and advocating a minimalist approach to revision of the innocent spouse relief provision. This position was incorporated into the House version of the 1998 Act.

In the Treasury's view, as explained in its report, the most effective way to deliver relief to taxpayers who merited relief was to refine and simplify the then-existing rule and to improve the administration of the rule by the Service. It strenuously opposed recommendations to separate the liabilities of married taxpayers who had filed jointly. In the Senate Finance Committee hearings held in February, 1998, a series of cases demonstrating how poorly the relief provision worked undermined the Treasury's argument, and ultimately was persuasive in the Finance Committee's decision to adopt the substance of the ABA recommendation. Its provision would have extended relief to all spouses, whether they remained married or not, for all unpaid taxes, including assessed taxes. The Senate legislative language, however, imposed a number of restrictions and "hooks" intended to prevent married taxpayers from using a provision intended for relief to shield assets from efforts to collect legitimate tax liabilities. Many senior members of the tax bar shared the Treasury's view that the Senate provision was an invitation to tax avoidance, with married taxpayers converting joint return liabilities into separate liabilities and transferring assets into joint names which would be difficult for the IRS to reach as a creditor. Indeed, the Senate provision was "scored" for budgetary purposes at a very high number because of concern that it would facilitate legitimate tax collection and cause serious revenue loss for that reason. This scoring would make acceptance of the Senate version problematic.

The Conference on the 1998 Act compromised by accepting both the House and the Senate version of the bill, and by adding an equitable catchall which the legislative history describes as intended to provide relief for liability for unpaid assessed tax. In providing a three-step relief formula, the Conference Committee sought to provide relief where it was most needed (for divorced, widowed or separated spouses) and yet limit the adverse impact of expanded relief on tax collections. There are, however, widely divergent views on what actually was accomplished, and a lingering doubt as to just how far the relief does extend. The Service, which acted promptly in issuing a revised Form 8857 (Request for Innocent Spouse Relief) and its accompanying IRS Publication as well as Guidance for the administration of the new equitable relief provision, continues to employ concepts that hark back to the now superseded innocent spouse provision.

Relief after IRS Restructuring

The 1998 Act, enacted on July 22, added new Code Sec. 6015, which now provides three separate means of obtaining relief from joint and several liability for tax on previously filed joint returns. The 1998 Act required the IRS to develop and publish a form by which taxpayers could apply for relief within 180 days (January 19, 1999), which it did, using the original Form 8857 as a model. This form makes plain that all three relief provisions may be available to each claimant, and all of them can be requested seriatim on the same form. For purposes of this discussion, these relief routes will be considered as they are provided in the statute. First, I consider a preliminary issue which may affect situations in which relief would (or should) otherwise be available.

Relief Limited to Unpaid Taxes

The Service has taken the position in its Guidance for the application of the equitable relief catch-all that these relief rules apply only to
taxes that have not been paid.\textsuperscript{38} The statute itself seems to preclude all refunds from the election to separate liabilities,\textsuperscript{39} although refunds should be allowed for relief from liability for deficiencies through an innocent spouse election. Denial of relief in all cases when payment has been made is a harsh rule which does have antecedents in the legislative history,\textsuperscript{40} but, as a blanket requirement before requests for relief can be considered, seems unjustified.

Innocent spouse relief is now, as it was originally, a collection issue. Whether relief from joint liability should be extended to a taxpayer who had signed the joint return often arose for the first time when the Service began collection activity against him or her. This seems to have been a frequent problem for divorced or separated taxpayers, who were unaware that the return had been audited and that a deficiency had been assessed.\textsuperscript{41} The audit having been concluded with the other spouse, who may not have effectively resisted the assertion of the deficiency, the Collection Division would then pursue the taxpayer for no reason other than he or she was easier for it to find. At that point in the proceedings the taxpayer against whom the liability was asserted may not have been aware of his or her ability to obtain innocent spouse relief, and some part of the asserted liability may in fact have been paid before an effective request for relief was made.\textsuperscript{42}

Should that fact disqualify the taxpayer from these relief provisions? It did not seem to preclude relief under the pre-amendment innocent spouse rule, and similarly should not for relief requested under Code Sec. 6015(b). The statute provides that “the taxpayer shall be relieved of liability” under the appropriate circumstances, without reference to payment.\textsuperscript{33} Code Sec. 6015(c) (the election to separate liabilities) provides that “the taxpayer’s liability for any deficiency which is assessed … shall not exceed …” the taxpayer’s allocable portion of the liability, and Code Sec. 6015(f) refers to relief from liability for any “unpaid tax” as well as deficiencies.\textsuperscript{44} Authorization of refunds in Tax Court proceedings has now been limited to innocent spouse and equitable relief, specifically excluding relief asserted by the election to separate liabilities,\textsuperscript{45} but this rule does not preclude refunds under other procedures.\textsuperscript{46} Finally, the innocent spouse amendments are effective for liabilities arising before the effective date (July 22, 1998) but only if they remain unpaid on that date.\textsuperscript{47}

Because of the difficulty many taxpayers have faced in sorting out their liabilities on a joint return for items over which they did not have control, relief should not be so limited. The ABA Recommendation did take the position that a previously paid assessed tax should not be refunded under its proportional liability proposal. Married taxpayers may often make bargains in deciding which spouse should pay the income tax with the return as filed, and later occurrences which result in a greater liability than that bargained for should not upset the earlier bargain. But payment of the deficiency asserted at a later time would not generally be part of that bargain and may result from circumstances which apply only to the payor. Under those circumstances, the later payment of all or part of the deficiency should not disqualify the taxpayer’s request for relief from liability for that deficiency.

**ELECTING RELIEF**

A married taxpayer may “elect to seek relief under the procedures prescribed”\textsuperscript{48} for the traditional innocent spouse rule.\textsuperscript{49} The elements for relief are generally the same as they were in prior law, shorn of the requirement that the reporting of an item other than an omission be “grossly erroneous” or the numerical limits imposed in the 1984 amendments.\textsuperscript{50} In seeking this relief, therefore, the claimant must “establish” that he or she “did not know, and had no reason to know, that there was …” the understate-ment (or a portion of the under-state-ment) causing the tax liability.\textsuperscript{51} This requirement, a vestige of which continues to worry taxpayers who claim separation of liability,\textsuperscript{52} has always been the major impediment to relief. In addition, “it must be inequitable” to hold the claimant liable.\textsuperscript{53} Because these elements of the availability of relief are the root of the problems in obtaining that relief under the pre-amendment law, obtaining relief under the stripped down provision may be just as difficult as before unless more careful administration and the establishment of consistent standards for relief make the requirements clearer and therefore easier to meet. This is a very real possibility as the suspension of collection activities following an application for relief\textsuperscript{54} and the ability of the claimant to obtain a determination in the Tax Court will mean that the IRS cannot simply ignore requests for relief, as frequently happened in the past.\textsuperscript{55} But that possibility will be realized only in the long term, as claims for innocent spouse relief are made and determined. The well known problems with this provision are likely to persist, at least for awhile.

Relief is elective.\textsuperscript{56} An election by the taxpayer to claim relief from joint liability with respect to a joint return under of these provisions does not relieve the taxpayer’s spouse from joint liability. The ne-
cessity for having made an affirmative election at some point may be awkward when the taxpayer decides to seek relief when the substantive tax issues are in litigation. IRS representatives have said that requests for relief from joint liability when the case is in that procedural posture will be referred to Appeals. No reason appears why the existence of election procedures should prevent some common sense way of proceeding by incorporating the request for relief into the conduct of the litigation.

The timing of the election is another matter. Because the statute specifies only a limitation on how late the election may be made, not how soon, there is serious gap in understanding about the purpose of the election. This issue is more relevant to an election to separate liabilities, and will be discussed in part II. It is worth noting at this point that the election may not be made later than a date which is two years after “collection activities” have “begun . . . with respect to the taxpayer making the election . . .”.\(^5\) “Collection activities” are described in the legislative history as efforts by the Commissioner to enforce collection, as by garnishment of wages or a proceeding in court to enforce a lien.\(^6\) These efforts to collect tax are distinguished from the determination of a deficiency, the sending of the requisite statutory notice, and even, apparently, a demand for payment following assessment of the tax. When the Service has taken these steps, most taxpayers are aware of impending liability and might be expected to make the election to request relief from liability.\(^6\)

Once the election is made, the Service is restricted from undertaking the very collection activities (enforcement of liens and levies in court proceedings) which might invoke the two year limitation period.\(^6\) If a taxpayer who first elected to request relief as an innocent spouse later qualifies to elect separation of liability because divorce has become final or a spouse has died,\(^6\) the original election should be appropriately modified to allow separation of liability, even though this relief is more far-reaching than was the innocent spouse election, and even when the two year election period might have expired.\(^5\)

IRS determinations on relief for both innocent spouse and separation of liability will now be subject to review in the Tax Court,\(^4\) an entirely new procedure which will be discussed in part II.

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**ENDNOTES**


2 The Treasury’s report on various relief proposals makes as good a case for the “need” to impose joint liability for income tax due with respect to joint returns. Treasury Department Report on Joint Liability and Innocent Spouse Issues, released Feb. 10, 1998. See BNA, 1998 Daily Tax Report No. 29, pp. L-1 - L-27 (Feb. 12, 1998); 98 TNT 28-14, Doc 98-5641. The concern as expressed there and in less formal discussions of the problem is that taxpayers with assets will transfer assets generated by the tax savings into forms of joint ownership which can be attacked only with difficulty to collect individual debts of either spouse. If tax liability is transformed into the individual liabilities of the spouses who were “responsible” for tax generating items on the joint return, asset strategies could defeat efforts to collect tax legitimately due. The ABA report and others have expressed skepticism about these assertions, which are essentially unprovable ex ante.


4 Former Code Sec. 6013(e) (1954 Code): relief was extended only to liabilities for deficiencies resulting from omissions from income. The taxpayer requesting relief had to “establish” that he or she did not “know and had no reason to know” of the item, and that it would be “inequitable” to impose liability on him or her. These provisions fit the actual case quite nicely.


7 The statute also imposed numerical restrictions. The deficiency had to exceed $500 before relief would be available; and the deficiency had to exceed a stated percentage of the taxpayer’s adjusted gross income for the year when the deficiency was later asserted. The latter restriction, apart from being irrelevant to the substantive issue, posed serious problems of fairness. For a full discussion of these provisions, see Jerome Borison, Innocent Spouse Relief: A Call for Legislative and Judicial Liberalization, 40 Tax Law. 819 (1987). The old adage, “ignorance of the law is no excuse,” expressed the government’s concern. A taxpayer who it was thought to be conceded had a legitimate liability for tax on the return could not be excused for mere errors, whether of the recordkeeping variety (failure of proof) or for mistakes of law. Although ignorance was not supposed to be equivalent to innocence (a concept still at play in these provisions), many times the liability was asserted after a divorce or death. In that case, the taxpayer who applied for relief simply did not have proof either to contest the liability itself or its “grossly erroneous” nature. It must have been obvious very early in the game that the “grossly erroneous” standard was a legislative misstep, but it took deeper concerns before the that requirement was wiped away.


See Beck II, supra note 9 (turning wives into supplicants who deme themselves by showing how helpless and ignorant they were). Compare Friedman, note 5, supra, and infra, note 12 (reasonable inquiry sufficient).

This remains a problem for taxpayers who have filed joint returns and who intend to remain married. Creative tax reporting by one of the spouses can cause serious financial problems for the other. A reasonable inquiry about matters shown (inadequately or incorrectly) on the return might be thought to protect the spouse not responsible for the tax problem from serious tax liability, but this merely raises the very issue which must be decided. That is, did the taxpayer learn enough to be aware of a potential problem yet sign the return anyway? If one searches for a standard strong enough to withstand collection efforts in such a case, one looks in vain. See, Friedman, note 5, supra; R.J. Resor, CA-5, 97-1 USST ¶ 50,416, 112 F3d 1256 (1997). Items completely omitted from the return do not pose the same problem. See M. Wilsell, CA-9, 96-2 USST ¶ 50,398, 90 F3d 1459 (1996).

ABA Tax Section Legislative Recommendations 1992-12, 1995-2 ABA Rep’ts., 8E. See Domestic Relations Committee, Tax Section, Individual Cmnts. on Liability of Divorced Spouses for Tax Deficiencies on Previously Filed Joint Returns (July 29, 1996), available in the Tax Notes database, Doc. No. 96-21343, 96 TNT 150-30 (Aug. 1, 1996) (appending the complete version of the committee report). The comments, but not the report, are reprinted at 50 TAX LAW. 395 (1997). The original report was based on research done by Professor Richard Beck, whose work appears in Beck I, supra, note 9. His research demonstrated that imposition of joint and several liability on spouses who file joint returns for each other’s tax liability is a unique (and, in his view, totally unwarranted) disadvantage imposed on married taxpayers under the United States income tax. Other income tax systems differ significantly in the advantages or disadvantages of marital status in reporting and payment of income tax liabilities, and the committee did not explore the ability of spouses in other countries to protect assets from the tax collector by, for example, putting in joint names. So, while the committee was skeptical about claims that reliance on marital property law to foil the tax collector would be widespread, nor was it able conclusively to refute these assertions.

Imposing joint and several liability for tax on a joint return is sometimes criticized because it is said to be based on a competing norm, that married persons “pool” or combine their resources. The “pooling” idea and its implications are discussed in Robinson & Ferrari, supra note 10, and authorities cited by them. Tax liabilities on pooled resources could be viewed as a liability of the combined enterprise, no matter how it arose. As I have already said, the source of the joint liability rule seems to be more in aid of collection of tax liabilities in a legal environment where property is often held jointly and cannot be reached, at least not without difficulty, by the creditors of one spouse. Viewed in this way, joint and several liability has nothing whatever to do with marital pooling as such.

See Treasury Report, supra note 2, at pp. 23-28, critiquing a proposal to Require married taxpayers to file as individuals.

The standard proposed was that used under then current law to allocate refunds between married taxpayers, and is known as the separate tax method. Rev. Ruls. 80-6, 7, 8, 1980-1 CB 296, 298. To make that determination is necessary to determine the separate return tax liability of each spouse as if they had filed separately. The committee thought that most taxpayers would not have significant difficulty in making the calculation, since most would be wage earners, but it was a significant complication.

In a proportional liability system, the liability of each spouse for the tax actually due is first determined. This is then compared to amounts actually paid, through estimated tax, withholding or crediting of overpayments. The spouse would then be liable for any net amount due, up to the actual amount of the liability on the return. If a spouse had paid more than his or her share, he or she would not be permitted to claim a refund of the excess amount paid, which, in effect, would reduce the tax liability of the other spouse. The justification for this approach, also adopted in the 1998 Act, is that payment of known liabilities generally is an arrangement already worked out by the spouses themselves, which should not be upset by a subsequently determined tax liability. This calculation is discussed the ABA Committee Report, supra note 13, and at notes 29-31.

Comments by the Administrative Practice Committee of the Tax Section, while the proposal was under consideration in Council of the Tax Section, demonstrated some serious flaws in the committee’s original proposal. After trying to work these out, the committee decided that the separation of liability approach was superior.

This knowledge element is centrally important when relief is considered under the equitable catchall provision of the new law, to be discussed in the second part of this article. Before the local examiner can grant relief under new Code Sec. 6015(f), the examiner must be persuaded that the taxpayer requesting relief did not know of the failure to pay, and “had a bona fide reasonable belief” that tax would be paid. See Internal IRS Procedures “Equitable Relief Under Internal Revenue Code (IRC) 6015(f),” issued December 11, 1998 ("Equitable Relief Procedures"). ¶ 4.A.2.B. There is some suggestion that some sort of certification to that effect be included in the file. Such evidence as, for example, the putative payor’s propensity to gamble away money in the payor’s possession, would, presumably, be a negative factor.

Taxpayer Bill of Rights 2, P.L. 104-166, 110 Stat. 1452, 1454 Cong., 2nd Sess. ¶ 401 (directing the Secretary of the Treasury and Comptroller General “to conduct separate studies” of certain aspects of joint and several liability, including “whether [the] innocent spouse [rule] provide[s] meaningful relief in all cases where relief is appropriate…”).


Treasury Report, note 2, supra, 57-58.

H.R. 2676, 105th Cong., 1st Sess. ¶ 321 (1997), as passed by the House. Basically, the House version would have eliminated the “grossly erroneous” test, removed the $500 minimum for relief, and repealed the pre-determination year limit on relief. Otherwise, the innocent spouse rule would retain the basic elements of (1) knowledge and (2) equity, with the burden of the taxpayer seeking relief to “establish” these elements. The House bill also would have allowed partial relief (the Wilsell rule), imposed certain administrative requirements on the Service, and established a right to seek a determination on relief from the Tax Court, with collection efforts suspended while the case was pending.

Innocent spouse relief is a collection issue; the problem surfaces for the first time, in most cases, when collection efforts are undertaken by the Service against the spouse seeking relief. In a report prepared contemporaneously with the Treasury Report, the GAO found that administration by the Service of requests for relief was uncertain, inconsistent and basically standardless. Tax Policy: Information on the Joint and Several Liability Standard, GAO, GAO/GGD-97-34 (March 1997). There were then no estab-
lished procedures for proper review of innocent spouse cases. The Treasury believed that improving the administration of requests for relief, with a form setting out the requirements for relief and centralized review to establish consistent standards would deal with most problems, and that broadening the substantive test was a prescription for trouble. The form for requesting relief, Form 8857, was first released in March 1998.


27 These restrictions were retained in Code Sec. 6015 as enacted, and will be discussed in part II. One of the most important restrictions would disqualify an election to separate liabilities under Code Sec. 6015(c) to taxpayers who "the Secretary demonstrates ... had actual knowledge [at the time the return was signed] ... of any item giving rise to a deficiency ... " Code Sec. 6015(c)(3)(C).

28 Most common debts, such as credit card debts, real estate mortgages, home equity loans, loans to purchase durable goods, are joint and several. If taxpayers could unilaterally convert income tax liabilities into separate liabilities, the IRS would have an inferior position as a creditor. This was thought to be enough incentive to lead to widespread shifting of ownership into a joint format. The ABA committee was asked to consider this question, but was not able, given time constraints, to undertake a full investigation of the problem. These techniques are available now, and their use is probably inhibited, at least at upper income levels, by estate planning considerations. In any event, these practices are not widely observed. To think that many more taxpayers would take these steps, even contrary to self-interest, specifically to thwart collection of legitimate tax liabilities, is a dismal view of human nature.

29 Joint Committee estimated revenue loss from the revision of the "innocent spouse" provision at $1.3 billion for the five year window; only the suspension of interest and penalties scored higher. JCX-22-98 (March 31, 1998).


31 Id., p. 254.

32 New Code Sec. 6015 is a complicated provision which deals with difficult administrative issues in new and uncharted ways. There are gaps in the statutory coverage, and some new terminology is employed. There is going to be, quite obviously, a break-in-period of some duration.

33 Notice 98-61, 1998-51 I.R.B. 13. At the mid-year meeting of the Tax Section, representatives of the Internal Revenue Service released the "Equitable Relief Procedures," supra note 19, which contain an administrative structure meant to facilitate the development of consistent standards for application of equitable relief by centralizing the review function in the Atlanta office. The internal guidelines generally restate the standards discussed in the Notice, although these provisions do attempt to separate requests for which relief is "appropriate" from all other requests. Local examiners are generalized to grant relief (limited to unpaid tax reported on a filed joint return) without centralized review in such cases. All other cases (including deficiency cases of which do not qualify under the innocent spouse rule) must be submitted for review. These procedures will be extensively discussed in the second part of this article.

34 The short time fuse provided in the 1998 Act for the issuance of guidance made use of these concepts inevitable. As experience is gained from administration of these provisions, the old innocent spouse ideas will hopefully be replaced with more appropriate rules.

35 Former Code Sec. 6013(e), providing relief for innocent spouses, was repealed. Act §3201(e). The Act also provided that taxpayers seeking relief from joint and several liability could obtain determinations in the Tax Court. Code Sec. 6015(e). This provision will be discussed in part II.

36 Act §3201(c): "The Secretary of the Treasury shall develop a separate form with instructions for use by taxpayers in applying for relief ... " (Emphasis supplied.) Treasury representatives would surely agree that the current version of this form is simply the first cut at the problem, which, as will be seen, is made difficult by complex and inadequate statutory drafting, not to mention the inherent complexity of situations in which relief is likely to be requested.

37 Code Sec. 6015(a): applicant may claim relief under paragraph (1) (traditional innocent spouse relief), and "in addition to" traditional relief under paragraph (1), may "elect to limit such individual's liability for any deficiency ... " by separating the claimant's liability from that of his or her spouse with respect to the other joint return in question. Although equitable relief is not included within the sweeping language of subsection (a), it is also generally available. The Form states that the IRS "will automatically consider whether you [the claimant] qualify ..."

38 Notice 98-61, supra note 33, section 1.01(a). The two limited exceptions refer to the lead-in period (payment on or before April 15, 1999), provided to make sure taxpayers who might otherwise qualify for relief are aware of the requirement, and to payment of an installment required under an installment agreement with the IRS.

39 The Tax Court is authorized to allow or make credit or refund "to the extent attributable to the application of subsection (b) [innocent spouse relief] or (f) [equitable catch-all]," Code Sec. 6015(e)(3)(A). In the original Act, credit or refund was authorized for relief attributable to this section, which included separation of liability (relief provided under subsection (c)). The reference to subsection (c) was eliminated by a technical amendment made by the Trade Extension Act in October, 1998. Trade Extension Act of 1998 § 4002(d)(2), P.L. 105-277, 112 Stat. 2681 (Oct. 21, 1998). According to the Committee Report, this change was made to make clear that the ability to obtain credit or refund is "limited to" innocent spouse relief and the equitable catch-all. H.R. Rep. No. 105-817, 105th Cong., 2nd Sess. at p. 64 (1998). This history does concede that refund is possible for payment of a deficiency by a taxpayer who subsequently is found to qualify as an innocent spouse.

40 See S.Rep. No. 105-174, 105th Cong., 2nd Sess., at p. 56 ("liability for unpaid taxes") (1998); Conference Report, supra note 30, at p. 254 ("the conference intends that [equitable authority] [to provide relief] be used where ... it is inequitable to hold an individual liable for ... unpaid tax or deficiency ... ").

41 This situation occurred so often, with the IRS making substantive assertions (the audit) against one spouse but collection efforts against the other, that the IRS Restructuring Act specifically requires the Service "send any notice relating to a joint return ... separately to each filer." (Emphasis supplied.) Act, § 3201(e). This mandate is qualified that IRS should do so "whenever practicable." Presumably, this means that notice must be sent unless the taxpayer to whom it would be sent cannot be located, and that would almost never be true for the taxpayers who are requesting relief under these provisions.

42 Payment can occur in several different ways, including attempted compromise of the liability. One way is IRS application of a refund from a different year against the liability from the joint return year. See Code Sec. 6402(a). Another situation may arise when release of a lien or prevention of a levy may
be necessary. The taxpayer may not have had time to consider other options before making payment, so the request for relief may actually have come at a later time.

Claims for refund on the basis that there was no liability to pay the tax because of the application of the innocent spouse rule of former Code Sec. 6013(e) have been infrequent, but are not unknown. The Committee Reports also describe these provisions as relief from "unpaid taxes," but the discussion in the Reports does not make payment a reason for the blanket denial of relief. "Deficiency" is a technical term defined in Code Sec. 6211 which means liability for the tax imposed with respect to the return over the previously reported and assessed. It does not refer to payments. The innocent spouse provisions refer to "understatements" as defined in the penalty rules, Code Sec. 6662(e)(2)(A), but this definition merely compares the liability actually imposed with the liability reported on the return. Code Sec. 6015(b)(5) imports this statutory technique, Code Sec. 6015(b)(3), but it does not seem to have any technical function from the meaning of the term "deficiency." If anything, the use of this terminology seems to cut against attributing significance to payment of any part of the deficiency in question.

Note 39, supra.

See Code Sec. 6015(e)(3)(C) (refund suit filed by either individual on joint return may limit Tax Court jurisdiction).

Act §3201(g)(1). This provision cuts both ways. If it was necessary to single out for retrospective relief only those liabilities which had not been paid, then, presumably, prospective relief should be more widely available.

Code Sec. 6015 generally talks about "procedures," rather than the more traditional expression, "regulations." Treasury and IRS representatives have stated that the different language in this provision has no significance. Perhaps, this way of expressing the options available to taxpayers was meant by the draftsmen to distinguish "substantive" liability; perhaps, it was meant to give the Treasury more flexibility to create the procedures quickly and efficiently, without having to resort to the notice and comment process under the Administrative Procedure Act. The Internal Revenue Service has always had that much authority in any event, although its "procedures" do not have the force and effect of law. Legal hairsplitting about the amount of authority conferred on the IRS should not be important in providing assistance to taxpayers who need help. The IRS has also taken the position that determinations made under the equitable catch-all provision are not reviewable. It is likely, however, that, at some point, judicial review will occur for abuse of discretion. This issue is discussed in part II.

Code Sec. 6015(b).

In this discussion, I do not mean to belittle the very real improvements to the innocent spouse rule from eliminating these basically irrelevant and certainly complicating limitations. It is now simpler and more direct, and that is an improvement.

Code Sec. 6015(b)(1)(C). In addition, the statute will now permit partial relief when the taxpayer knew (or should have known) about a portion of the understatement in tax but not all of it. Code Sec. 6015(b)(2). This provision is intended to incorporate the holding of Wksell supra note 12. Again, the taxpayer is required to "establish" the extent of her lack of knowledge, a practically impossible burden, and, in reality, invites the court to do equity in cases where there is some but not total awareness.

See note 27, supra.

Code Sec. 6015(1)(D). The "equitable nature of innocent spouse relief is echoed in the equitable catch-all provided by Code Sec. 6015(f). The Service has published "interim guidelines" on how it expects to administer the equitable relief provision, and as these guidelines evolve, they will quite likely come to reflect its view of the equities in the innocent spouse rule itself. See Notice 98-61, note 33, supra. Moreover, the Service has issued the Equitable Relief Procedures as an internal memorandum, explaining the procedures for obtaining a set of consistent rules in the administration of equitable relief. See note 19, supra. While there is no provision as yet for the dissemination of decisions, the procedures can only be effective if there is some way to communicate these decisions to the field. At some time, these should be a fertile source for principles governing both relief provisions.

Code Sec. 6015(e)(1)(B).

Despite IRS statements that this was not so, the GAO found otherwise. GAO Report, supra note 24. Stated differently, the standards applied were so inconsistent, and centralized review did not exist, that the treatment of many such claims was tantamount to ignoring any substance they might have contained. These claims, after all, were often made in response to IRS efforts to collect an assessed tax.

Code Sec. 6015(b)(1)(E); Conference Report, supra note 30, at p. 252.

Code Sec. 6015(b)(1)(E).

Id.


This may not always be the case, particularly in a divorce situation where the spouse responsible for the tax reporting problem may have agreed in a divorce instrument to accept responsibility for the tax consequences of having reported the transaction incorrectly. Such agreements do not bind the Service and, in any event, could not prevent it from taking collection actions against the taxpayer. It is only when those collection actions become directly personal will some taxpayers fully understand the extent of their exposure to liability. It is interesting to note that the Service will now consider divorce agreements allocating responsibility for tax liabilities between the spouses as a factor in deciding whether to give equitable relief under the catch-all provision. See Notice 98-61, note 33, supra, at section 3.01(1)(d).

Code Sec. 6015(e)(1)(B)(i).

It is an interesting feature of Code Sec. 6015 that the nature of relief available to the taxpayer can change with events occurring after the taxable year to which the tax liability relates. In a particularly difficult situation, the taxpayer may even have strong incentives to pursue a divorce, or at least a separation, in order to escape liability for income tax on his or her spouse's transaction. There are a number of limitations or restrictions on relief, however, to suggest that divorce to escape tax liability may not be as straightforward as it appears.

Treasury representatives have indicated their expectation that taxpayer elections will be modified as necessary with the assistance of IRS personnel to provide the information required to make the election effective. Moreover, the Form itself anticipates the election of all possible forms of relief in a single filing. If all this is true, and flexibility is the order of the day, there is no apparent reason why a taxpayer could not modify his or her election as often as necessary to make it effective.

Code Sec. 6015(e)(1). But not determinations under Code Sec. 6015(b) (requests for equitable relief). See note 19, supra. An interesting aspect of these rules is that Tax Court is expressly granted authority to allow refunds "to the extent attributable to the application of subsection (b) or (f)." (Emphasis supplied.) Code Sec. 6015(e)(3)(A). See note 48, supra.
New Burden of Proof

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cess. In some instances the government or the taxpayer may be willing to concede (subject to the court's ultimate acceptance) the burden of proof issue in the particular case. Alternatively, the parties should attempt to stipulate which requirements the parties agree have been met and which are still in dispute. Such stipulations would streamline the process and avoid unnecessary costs and waste of judicial resources.

Conclusion

While popularly acclaimed, the burden of proof provision fails to live up to its advertised promise. It simply contains too many limitations and qualifications. As a result, the costs of the provision clearly outweigh its benefits. The new legislation is likely to cause the IRS to become more intrusive. It also will increase the costs of tax controversies and tax judicial resources. Proponents of the provision have yet to demonstrate that the provision is a bill of rights for taxpayers as opposed to a bill of goods.

ENDNOTES

1 Exceptions to general rule. The Internal Revenue Code (the "Code") contains a number of civil provisions that explicitly place the burden of proof on the IRS: (1) fraud (Code Sec. 7454(b)); (2) required reasonable verification of information returns (Code Sec. 6201(d)); (3) foundation managers (Code Sec. 7454(b)); (4) transferor liability (Code Sec. 6902(a)); (5) review of jeopardy levy or assessments procedures (Code Sec. 7429(g)(1)); (6) property transferred in connection with performance of services (Code Sec. 83(d)(1)); (7) illegal bribes (Code Secs. 162(c)(1) and 162(c)(2)); (8) golden parachute payments (Code Sec. 280G(b)(2)(B)); (9) unreasonable accumulation of earnings (Code Sec. 534); (10) expiration (Code Sec. 877(e)); (11) public inspection of written determinations (Code Sec. 6110(h)(4)(A)); (12) penalties for promoting abusive tax shelters (Code Sec. 6703(a)); (13) income tax return preparers' penalty (Code Sec. 7427); (14) status as employees (Sec. 530 of the Revenue Act of 1978 (P.L. 95-600)).


The Internal Revenue Service Restructuring and Reform Act contained the Taxpayer Bill of Rights III ("TBOR3").

5 See Danville Plywood Corp., CA-FC, 90-1 ustc ¶50,161, 899 F2d 3, aff'g 503 F3d 10,161, 899 F2d 3, aff'g CisCl, 89-1 ustc ¶9248, 16 CisCl 584.


See Code Sec. 7491(a)(1), et seq.

See Code Sec. 7491(a)(2)(a).

9 See Code Sec. 7491(a)(2)(b).

10 See id.

11 See Code Sec. 7491(a)(2)(C).


13 See id.

14 Code Sec. 7491(a)(1).


16 See, e.g., Tax Ct. R. Prac. 90.

17 Code Sec. 7491(a)(1).

18 See Code Sec. 6902(a).

19 See Code Sec. 7454(b).


21 See id.

22 See id.

23 See id: Code Sec. 7491(a)(2)(B).

24 See id; see, e.g., Nissel Sangyo America, Ltd., DC-III, 95-2 ustc ¶50,327.


26 See id.

27 See id.


29 See Code Sec. 7491(a)(3).

30 See Code Sec. 7491(b); S. Rep. No. 105-174.

31 See Code Sec. 7491(c).


33 See, e.g., Tax Ct. R. Prac. 24(3), regarding conflicts of interest where counsel is a potential witness in a case.
Global Interest Netting in the Wake of Rev. Proc. 99-19

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