



Appeal of Juan F. and Elizabeth M. Lopez

Year	<u>Additional Tax</u>	<u>Fraud Penalty</u>	<u>Total Proposed Assessment</u>
1974	\$ 483.38	\$241.69	\$ 725.07
1975	968.00	484.00	1,452.00
1976	1,083.15	541.57	1,624.72

The sole issue presented by this appeal is whether appellants have established error in respondent's proposed assessments of additional personal income tax and in respondent's proposed penalties for the years in issue.

Any references to appellant shall mean appellant Juan F. Lopez. Any references to appellants shall mean appellant Juan F. Lopez and appellant Elizabeth M. Lopez.

During the years 1973 through 1977, appellant was the Director of Manpower of the Office of Equal Opportunity for the City of Oakland, California. In 1973, appellant arranged for Lucy Mayorga to be hired by the City of Oakland under the alias of Patricia Gomez. Shortly thereafter, appellant had Lucy Mayorga open a joint account (joint account) with appellant's wife, Elizabeth M. Lopez. The joint account was opened in the names of Elizabeth Sanchez (appellant's wife's maiden name) and the alias Patricia Gomez. By the end of 1973, Lucy Mayorga, alias Patricia Gomez, no longer worked for the City of Oakland. Appellant, however, arranged for the name Patricia Gomez to remain on the payroll of the City of Oakland. Appellant has admitted that, during the years 1974 through 1977, he received the Patricia Gomez payroll checks, personally forged her signature on them, and caused them to be deposited into the joint account. Thereafter, appellant used the money for his own purposes, but did not include the amounts in gross income on the joint personal income tax returns which he and his wife filed for the years 1974 through 1977. During the years 1975 through 1977, appellant filed for California income tax refunds under the name of Patricia Gomez. Respondent approved the refunds to the alias Patricia Gomez and issued refund checks in her name. Appellant received these refund checks, endorsed them, and deposited them into the joint account.

Appellant also admitted that during the period between August 1975 and July 1976, he received one-half of the net income of an employee under his direction named Martha Trujillo. Appellant admitted that Martha

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'Trujillo was required to make these payments to him as a condition of her employment with the department. Appellants did not include these amounts in gross income on their tax returns.

Respondent determined appellants' unreported taxable income for the years 1974, 1975, 1976, and 1977 to be **\$6,911.46, \$10,910.55, \$10,903.48, and \$9,877.00**, respectively. Respondent gave appellants credit for the taxes paid under the name of Gomez, but assessed a 50 percent fraud penalty.

On April 13, 1979, respondent issued notices of proposed assessment for the years 1974 through 1977. Appellants protested the proposed assessments for the years 1974 and 1977. The proposed assessments for 1975 **and** 1976 were not protested, and **therefore, became final** 60 days after they were mailed. (Rev. & Tax. Code, § 18591.) After due consideration, respondent affirmed its assessments for the years protested, but by mistake issued notices of action for the years 1974 through 1977. On the basis of these notices of action, appellants appeal respondent's assessments for the years 1974, 1975, and 1976.

Appellants contend that they filed timely protests of respondent's notices of proposed assessment for the years 1974 through 1977. Respondent contends that this board has no jurisdiction over the appeals for the years 1975 and 1976 on the grounds that the assessments for those years are final. Section 18590 of the Revenue and Taxation Code provides, in pertinent part, that within 60 days after **the** mailing of each notice of proposed assessment, the taxpayer may file with the Franchise Tax Board a written protest of the proposed assessment. Section 18591 of the Revenue and Taxation Code provides, "**[i]f** no protest is filed, the amount of the deficiency assessed becomes final upon the expiration of the 60 day period." The record indicates that appellants timely protested the notices of proposed assessment for only the years 1974 and 1977. Appellants have not presented evidence to support their contention that protests were filed for 1975 and 1976. Therefore, under section 18591, the assessments for the years 1975 and 1976 became final 60 days after the notices of proposed assessment were mailed; In this case', the word "final" means an appeal to this board under section 18593 is foreclosed,- (Appeal of Frank Edward and Florence Hess, Cal. St. Bd. of Equal., Feb. 17, 1959.) Thus, it is apparent that this board has no jurisdiction over the

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appeals for the years 1975 and 1976. Appellants did not appeal the notice of action for the taxable year 1977. Consequently, this board may only consider appellants' appeal of the notice of action for the taxable year 1974.

Appellant also alleges that respondent's assessment for 1974 is barred by the statute of limitations. We do not agree. According to the provisions of sections 18586 and 18588 of the Revenue and Taxation Code, respondent is authorized to issue a notice of proposed assessment of additional tax for a given year at any time within four years after the last day prescribed by law for the filing of a personal income tax return for that year. (Appeal of Robert A. and Dorothy L. Craft, Cal. St. Bd. of Equal., Sept. 30, 1980.) The ~~normal~~ **four-year limitation** period for ~~assessing~~ a deficiency for taxable year 1974 expired on April 15, 1979. Respondent's notice of proposed assessment against appellant for 1974 was issued on April 13, 1979, within the allowable statutory period. We conclude, therefore, that appellant's allegation is without merit.

Appellant's wife, citing section 18402.9 of the Revenue and Taxation Code, submits that she should be relieved of liability for the assessment of tax.. Section 18402.9 of the Revenue and Taxation Code provides, in substance, that a spouse who files a joint return will be relieved of liability for the tax arising from a failure to report an amount of gross income if: (1) the omitted amount is attributable to the other spouse and constitutes more than 25 percent of the amount of gross income stated in the return; (2) the innocent spouse establishes that in signing the return she did not know of, and had no reason to know of, such omissions; and (3) it is inequitable to hold the innocent spouse liable for the tax, taking into account all of the facts and circumstances, including whether or not she benefited significantly from the omitted income. In support of her position, appellant's wife declares that she did not know, and had no reason to know, that taxable income was omitted from the return. Furthermore, appellant's wife declares that she did not benefit directly or indirectly from the items omitted from gross income, and it would be inequitable to hold her liable for the tax deficiencies in question. It is well established that the presumption that respondent's assessments of tax are correct is not overcome by mere unsupported statements. (Todd v. McColgan, 89 Cal.App.2d 509 [201 P.2d 414] (1949); Appeal of Shirley Mark, Cal. St. Bd.

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of Equal., Aug. 16, 1979.) The only evidence appellant's wife offers in support of her position: **are** unsupported self-serving statements. Consequently, we hold that appellant's wife does not qualify for relief under the "innocent spouse" provisions of section 18402.9.

The next issue presented by this appeal arises from appellants' assertion that **the assessment of additional** tax for the year 1974 should be withdrawn on the basis that it is arbitrary and erroneous. In support of this assertion, appellants contend that the 1974 assessment was not based on an audit of appellants' 1974 tax return, nor was it based on a federal determination of their tax liability. However, we cannot agree with the above mentioned assertion. The record indicates that respondent based its proposed assessments on the Patricia **Gomez tax returns** filed by appellant **and** on the payroll records of the City of Oakland for Martha Trujillo. Accordingly, we do not find respondent's proposed assessment for 1974 to be arbitrary, nor do we find it to be erroneous.

Revenue and Taxation Code section 18685 provides:

If any part of any deficiency is due to fraud with intent to evade tax, 50 percent of the total amount of the deficiency, in addition to the deficiency and other penalties provided in this article, shall be assessed, collected, and paid in the same manner as if it were a deficiency. In the case of a joint **return**, this section shall not apply with respect to the tax of the spouse unless some part of the underpayment is due to the fraud of such spouse.

Respondent alleges that appellants fraudulently underreported their taxable income for the year in issue. The burden of proving fraud is upon the respondent, and it must be established by clear and convincing evidence, something more than a slight preponderance of the **evidence**. (Valetti v. Commissioner, 260 F.2d 18'5, 188 (3d Cir. 1958); Appeal of Hubbard D. and Cleo M. Wickman, Cal. St. Bd. of Equal., Feb. 2, 1981.) Fraud is actual, intentional wrongdoing, coupled with a specific intent to evade a tax believed to be owing. (Appeal of Eli A. and Virginia W. Allec, Cal. St. Bd. of Equal., Jan. 7, 1975.) It implies bad faith and a sinister motive. (Jones v. Commissioner, 259 F.2d 300, 303 (5th Cir.

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1958).) Although fraud may be established by circumstantial evidence (Powell v. Granquist, 252 F.2d 56, 61 (9th Cir. 1958)), **it is never** presumed, and a fraud penalty will not be sustained upon circumstances which, at most, create only a suspicion. (Jones v. Commissioner, supra; Appeal of Hubbard D. and Cleo M. Wickman, supra,)

Appellants contend that the evidence offered to this board by respondent is inadmissible hearsay. According to regulations on the hearing procedures of this board, hearsay evidence is admissible, "if it is the sort of evidence on which responsible persons are accustomed to rely in the conduct of serious affairs." (Cal. Admin. Code, tit. 18, reg. 5035, subd. (c).) Respondent offered hearsay evidence taken from an **official** police report as proof of appellants' fraudulent intent to evade taxes. This board has previously held that police reports were reliable evidence admissible on appeal in accordance with regulation 5035, subdivision (c). (Appeal of Jack Den Bleyker, Cal. St. Bd. of Equal., Nov. 14, 1979.) On the basis of the foregoing, we find that the evidence submitted by respondent was admissible in the appeal before this board.

The use of aliases is considered a "badge of fraud" indicating that the taxpayer filed false and fraudulent returns. (Paul Yu, ¶ 73,188 P-H Memo. T.C. (1973).) Appellant **used the alias** Patricia Gomez to obtain money from the City of Oakland and to obtain tax refunds from the Franchise Tax Board. In addition, a consistent pattern of underreporting large amounts of income over a period of years is substantial circumstantial evidence bearing upon the fraudulent intent to evade taxes due. (Holland v. U.S., 348 U.S. 121 [99 L.Ed. 150] (1954); J. K. Vise, 31 T.C. 220, 227 (1958).) The record indicates that appellant admitted to receiving unreported taxable income, varying from 34.8 percent to 27.8 percent of the reported taxable income for the years 1974 through 1977. Furthermore, appellant does not provide any explanation for these understatements of income. Circumstances such as these are strong indications of fraud. (J. K. Vise, supra.)

The record also indicates that we are dealing with an individual familiar with the law and its **requirements**. Appellant held a responsible government position and was clever and knowledgeable enough to have devised and carried out schemes to obtain unearned funds from a subordinate **employee and** from the City of Oakland. As a **part of** his initial scheme, appellant prepared and filed

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tax returns in the name of Patricia Gomez. This action reveals appellant knew the money paid to the alias Patricia Gomez was taxable. Appellant used this money for his own purposes and, therefore, must have known this money was taxable to him. Appellant, however, did not report it as a part of his taxable income. We find that these circumstances provide strong evidence that appellant intended to fraudulently evade taxes.

In a case somewhat similar to the second scheme formulated by appellant, the taxpayer originated a plan which embraced using his position in a company to obtain kickbacks which were deposited in bank accounts carried under fictitious names. The taxpayer used this money for his own purposes and did not report it as part of his gross income. After a finding that the taxpayer knew the kickbacks were taxable to him, the court held that the taxpayer was guilty of fraud with the intent to evade taxes. (Henry Naples, 32 T.C. 1090 (1959).) In his second scheme, appellant perpetrated this same pattern of fraud. Appellant used his position to obtain kickbacks which were deposited in a bank account carried under fictitious names. Appellant used the money for his own purposes and did not report it as part of his gross income. In view of the findings in our analysis of appellant's initial scheme, we hold that the circumstances merit a finding that appellant also knew the amounts obtained from his 'second scheme were taxable to him. In accordance with these findings, we conclude that appellant fraudulently underreported taxable income for the year in issue.

Appellant's wife argues that respondent has not met its burden of proving **she** committed fraud with intent to evade taxes due. **Respondent** submits that its burden of proof has been met. As presented earlier, section 18685 of the Revenue and Taxation Code provides that in the case of a joint return, the penalty for fraud shall not apply with respect to the tax of the spouse unless some part of the underpayment is due to the fraud of that spouse. Respondent argues that the scheme to defraud the City of Oakland and the State of California depended upon her actions. The only facts presented are that appellant's wife opened the joint account and that she signed the joint income tax return which was filed. We do not find this to be clear and convincing evidence of either intentional wrongdoing or a specific intent to evade a tax believed to be owing. These are circumstances which, at most, create only a suspicion. Accordingly, we hold respondent has not met

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◦ its burden of proving that appellant's wife is guilty of fraudulently evading taxes-for the **year** in issue. In so holding, we wish to make it clear that no part of the penalty is abated, **but** the innocent spouse is not liable for payment of the penalty. (Joseph D. Kwong, 65 **T.C.** 959 (1976).)

