

1 Louis A. Ambrose
 Tax Counsel IV
 2 Board of Equalization, Appeals Division
 450 N Street, MIC: 85
 3 PO Box 942879
 Sacramento CA 95814
 4 Tel: (916) 445-5580
 Fax: (916) 324-2618
 5

6 Attorney for the Appeals Division

7 **BOARD OF EQUALIZATION**

8 **STATE OF CALIFORNIA**

9
 10 In the Matter of the Appeal of:) **HEARING SUMMARY**
)
 11 **ROCHELLE M. DORFLER**) **PERSONAL INCOME TAX APPEAL**
)
 12 **(Party requesting innocent spouse relief)¹**) Case No. 306426
)

	<u>Years</u>	<u>Proposed Assessments²</u>
14	1988	\$ 11,867.00
15	1989	61,066.00
16	1990	120.00

17
 18 Representing the Parties:

19 For Appellant: C. Henry Veit, Attorney
 20 For Franchise Tax Board: Mark McEvelly, Tax Counsel III
 21

22 **QUESTIONS:** (1) Whether appellant timely filed a request for innocent spouse relief pursuant to
 23 Revenue and Taxation Code (R&TC) section 18533, subdivision (b)(1)(E).
 24 (2) Whether R&TC section 18533, subdivision (e)(3)(B), bars the Board from
 25

26
 27 ¹ Appellant resides in Reno, Nevada. Appellant's former husband (Elliott Dorfler) was notified of his right to join the appeal by letter dated April 18, 2005. Mr. Dorfler did not respond to that letter.

28 ² FTB will supply the amount of the interest accrued in this appeal on the date of the oral hearing.

1 reaching the merits of appellant's claim for innocent spouse relief, because the
2 Board already determined that appellant is not entitled to relief in a prior
3 proceeding for the same taxable years.

4 (3) If the Board is not barred from reaching the merits of appellant's claim, whether
5 appellant has demonstrated that she is entitled to innocent spouse relief.

6 HEARING SUMMARY

7 **I. Background**

8 This appeal arises from a factual background that raises procedural issues that the Board
9 must decide before reaching the merits of appellant's innocent spouse claim. The background is
10 outlined below:

- 11 • Appellant and her former husband filed joint returns for 1988, 1989, and 1990, reporting
12 adjusted gross income ranging from \$45,000 to \$65,000.
- 13 • On June 29, 1992, appellant's former husband pled guilty to embezzling \$1.7 million
14 from his employer and was sentenced to three years in prison.
- 15 • In 1993, respondent audited appellant and her husband, and determined that appellant and
16 her former husband failed to report the embezzlement income on their joint tax returns.
- 17 • On June 9, 1994, respondent issued Notices of Proposed Assessment (NPA's) for the
18 years at issue. Appellant timely protested the NPA's and requested innocent spouse
19 relief. Respondent decided to relieve appellant of the fraud penalties, but otherwise
20 denied her request for innocent spouse relief. Respondent issued Notices of Action
21 (NOA's) on June 26, 1995, reflecting its determinations.
- 22 • Appellant appealed to the Board. The Board held an oral hearing on October 10, 1996,
23 and sustained respondent's denial of relief on the same day. (Case No. 95A-0991; see
24 exhibit B to this Hearing Summary.) Appellant did not file a petition for rehearing and
25 the Board's decision became final.
- 26 • Shortly after the Board's decision, respondent began mailing standard billing notices.
27 Appellant did not make voluntary payments in response to those notices.
- 28 • In April 1999, respondent filed a state tax lien. Respondent then collected part of the

1 liability through wage garnishments in June 1999.

- 2 • At some point (the timeline is in dispute and will be discussed later) appellant made her
3 second request for innocent spouse relief. Respondent denied the request on January 28,
4 2005, and appellant filed this appeal. The outstanding liability remains mostly unpaid.

5 Because the parties' initial briefing did not include a detailed discussion of the procedural
6 issue, the Appeals Division requested additional briefing by letter dated May 4, 2007, in which the
7 parties were requested to discuss the following issues:

- 8 • Whether the Board has jurisdiction to hear this appeal pursuant to R&TC section 18533,
9 subdivision (e).
- 10 • Whether the two-year statute of limitations prescribed in R&TC section 18533,
11 subdivision (b)(1) applies to bar appellant's second request for relief and applies to
12 appellant's request for equitable relief under R&TC section 18533, subdivision (f).
- 13 • Whether the Board has jurisdiction to hear and decide appellant's request for equitable
14 relief in light of the Board's decision in the *Appeal of Patricia Tyler-Griffis* (2006-SBE-
15 004), decided on December 12, 2006.
- 16 • If the Board has jurisdiction to hear this appeal, whether the doctrine of res judicata
17 precludes the Board from reaching the merits of the appeal.

18 The parties submitted supplemental briefing but the matter was subsequently deferred
19 when respondent, in a letter dated December 6, 2007, requested that the Board postpone proceedings to
20 allow the parties to attempt to negotiate a settlement. The matter was deferred until November 5, 2008,
21 when respondent advised the Board Proceedings Division that the appeal would not be resolved through
22 settlement negotiations and requested that the appeal be reactivated and placed on calendar.

23 **Issue 1: Whether appellant timely filed a request for innocent spouse relief pursuant to R&TC**
24 **section 18533, subdivision (b)(1)(E).**

25 ***Contentions***

26 ***Appellant's Contentions***

27 Appellant contends that the Board has jurisdiction to hear this appeal because she timely
28 filed her request for relief within the time period specified in R&TC section 18533, subdivision

1 (e)(1)(A)(ii) and (iii). Appellant states that she “noted” the amendment to IRC section 6013 and the
2 corresponding amendment to R&TC section 18533 with respect to procedures for requesting innocent
3 spouse relief. For that reason, appellant asserts that she filed an IRS Form 8857 requesting innocent
4 spouse relief with respondent on September 21, 1999. Appellant states that she filed the IRS form
5 because respondent had not yet developed its own form. Appellant states that respondent commenced
6 collection activity in the spring of 1999 and appellant requested relief in September of 1999. Appellant
7 asserts that respondent acknowledged the request for relief by suspending collection activity as required
8 by R&TC section 18533, subdivision (e)(1)(B). (App. Supp. Br., p.2-3.) Appellant further states that
9 respondent had continuous communication with appellant prior to and after the enactment of the relevant
10 amendments to R&TC section 18533. Finally, appellant states that it appears that respondent has
11 waived the statute of limitations by attempting to resolve this matter on its merits. (App. Supp. Br., p.3.)

12 With respect to her request for equitable relief pursuant to R&TC section 18533,
13 subdivision (f), appellant contends that the Board held in *Appeal of Patricia Tyler-Griffis, supra* that it
14 had jurisdiction to consider such a request when the request also seeks traditional innocent spouse relief
15 under R&TC section 18533, subdivision (b). Because appellant’s request was timely filed and requested
16 innocent spouse relief under both provisions, appellant contends that the Board has jurisdiction to hear
17 her appeal. (App. Supp. Br., p. 4.)

18 ***Respondent’s Contentions***

19 Respondent contends that appellant’s request for relief was timely filed only if
20 appellant’s letter dated October 13, 1999, is determined to be an election for relief because that letter
21 raised the issue of the availability of innocent spouse relief in that letter. Respondent asserts that
22 appellant has the burden of demonstrating that she made a timely request for relief. (Resp. Supp. Br.,
23 p.2.) Respondent further states that if the Board finds that appellant filed a timely request for relief, then
24 the Board has jurisdiction to hear appellant’s request for equitable relief because it was coupled with a
25 request for traditional relief. (Resp. Supp. Br., p.3.)

26 ***Applicable Law***

27 There are three types of innocent spouse relief under R&TC section 18533: traditional
28 relief under subdivision (b), separate liability election under subdivision (c), and equitable relief under

1 subdivision (f). Appellant's second request for innocent spouse relief seeks traditional relief under
2 subdivision (b) and equitable relief under subdivision (f).

3 There are several requirements to obtaining relief under subdivision (b), each of which
4 will be discussed later. As relevant to this issue, subdivision (b) requires that the requesting spouse:

5 . . . elect the benefits of this subdivision not later than the date that is two
6 years after the date the Franchise Tax Board has begun collection
7 activities with respect to the individual making the election.

8 (Rev. & Tax. Code, § 18533, subdivision (b)(1)(E).) The foregoing language essentially creates a two-
9 year statute of limitations for requesting traditional relief under subdivision (b).³

10 Subdivision (f) does not expressly contain any statute of limitations for requesting
11 equitable relief. The federal counterpart, IRC section 6015(f), also does not contain any expressed
12 limitations period. However, the Internal Revenue Service (IRS) has stated that it will apply a two-year
13 statute of limitations in equitable relief cases. (Rev. Proc. 2003-61, 2003-2 C.B. 296, § 4.01(3).) While
14 it is clear that the Board is bound by federal innocent spouse regulations (see Rev. & Tax. Code, §
15 18533, subd. (g)(2)), and that federal precedent is applied extensively in California innocent spouse
16 cases (see *Appeal of Patricia Tyler-Griffis*, 2006-SBE-004, Dec. 12, 2006), it is not clear that the Board
17 is bound by federal administrative rulings, such as a revenue procedure.

18 It is well-settled law that the burden is on the appellant to prove issues of fact. (*Appeal of*
19 *Oscar D. and Agatha E. Seltzer*, 80-SBE-154, Nov. 18, 1980; *Appeal of Janice Rule*, 76-SBE-099, Oct.
20 6, 1976.) Appellant's failure to produce evidence within her control gives rise to a presumption that, if
21 provided, such evidence would be unfavorable to her case. (*Appeal of Don A. Cookston*, 83-SBE-048,
22 Jan. 3, 1983; *Giddio v. Commissioner* (1970) 54 T.C. 1530, 1535.) When respondent has no record of a
23 document being filed and the taxpayer does not present evidence to the contrary, the Board generally
24 concludes that the taxpayer did not file the document in question. (See *Appeal of Wing Edwin and Faye*
25 *Lew*, 73-SBE-053, Sept. 17, 1973.)

26 An administrative agency's jurisdiction depends upon the provisions of the statutes from
27 which its powers are derived, and the agency cannot validly act in excess of the limits of that

28 ³ Staff notes that, where collection activity begins after October 10, 1999, a four-year statute of limitations may apply. (Rev. & Tax. Code, § 18533, subd. (h)(2).) In this case, however, collection activity began prior to October 10, 1999.

1 jurisdiction. (*Flickenger v. Industrial Accident Commission* (1919) 181 Cal. 425; *Appeal of Nicholas*
2 *Schillace*, 95-SBE-005, Aug. 2, 1995.) In this case, the relevant jurisdictional provisions are found in
3 R&TC sections 18533, subdivision (e).

4 In general, when a taxpayer protests an NPA, respondent must reconsider the assessment
5 and act upon the protest (i.e., issue an NOA). (Rev. & Tax. Code, § 19044.) If the NOA affirms the
6 assessment, the Board has jurisdiction to hear an appeal if the taxpayer files the appeal with the Board
7 within 30 days. (Rev. & Tax. Code, § 19045.) The Board’s decision on the appeal becomes final 30
8 days from the date of the decision, unless a petition for rehearing is filed. (Rev. & Tax. Code, § 19048.)
9 If a petition for rehearing is filed, the Board’s decision becomes final 30 days from its decision on the
10 petition for rehearing. (*Id.*) A Board decision that has become final pursuant to statute “cannot be
11 reconsidered or changed.” (*Appeal of Philip and Adella Bloom*, 77-SBE-067, May 10, 1977.) Under the
12 general appeal provisions, the only mechanism for obtaining further review of a final assessment is for
13 the taxpayer to pay the outstanding liability in full and file a claim for refund. (Rev. & Tax. Code,
14 § 19322 et seq.)

15 Of relevance here, R&TC section 18533 sets forth the requirements for innocent spouse
16 relief under California law. Subdivision (b)(1)(E) provides that the individual must “elect the benefits”
17 of that subdivision not later than two years after the date respondent has begun collection activities
18 against that individual. Respondent’s denial of innocent spouse relief is “treated as” an action upon a
19 protest under R&TC section 19044. (Rev. & Tax. Code, § 18533, subd. (e)(1)(A)(ii).) The taxpayer
20 then has 30 days to appeal to the Board and the appeal is “treated as” an appeal under R&TC section
21 19045. (Rev. & Tax. Code, § 18533, subd. (e)(1)(A)(iii).) The foregoing provisions were added to
22 section 18533 in 1999⁴ after appellant had filed her first innocent spouse request for relief which was
23 made in her protest of the NPA in 1994 and her subsequent appeal from the NOA in 1995.

24 *Staff Comments*

25 When the Board hears and decides a typical appeal from an NOA, it is clear the Board
26 has no further jurisdiction over the matter once the Board’s decision becomes final. (Rev. & Tax. Code,
27

28 _____
⁴ Ch. 931, Stats. 1999, effective October 10, 1999.

1 § 19048; *Appeal of Philip and Adella Bloom, supra.*) Appellant’s first request for innocent spouse relief
2 was made in her protest of respondent’s NPA’s for the years at issue, and the Board considered her
3 request in her appeal from the NOA’s. The Board decided the appeal adversely to appellant on
4 October 10, 1996, and the decision became final 30 days thereafter. (Rev. & Tax. Code, § 19048.) At
5 that time, which was prior to the 1999 amendments to R&TC section 18533, appellant could obtain
6 further review only by paying the outstanding liability in full and filing a claim for refund. (Rev. & Tax.
7 Code, § 19322, et seq.)

8 After the enactment of the 1999 amendments to R&TC section 18533, appellant contends
9 that on September 21, 1999, she filed the IRS Form 8857 with an accompanying letter stating that she
10 elected the benefits of R&TC section 18533 as amended in 1999. The letter also set forth the reasons
11 appellant met the elements required for innocent spouse relief. However, respondent contends that
12 appellant first raised the issue of innocent spouse relief in a letter to respondent dated October 13, 1999.
13 Thereafter, according to respondent, on January 20, 2000 appellant sent another letter to respondent that
14 further inquired about appellant’s right to request innocent spouse relief. (Resp. Op. Br., exhibit I, p. 2.)
15 Respondent states that its legal department informed appellant in a letter dated September 3, 2003, that
16 she had not “meaningfully participated” in the original protest and appeal so that she would be afforded
17 the opportunity to request innocent spouse relief under the 1999 amendments to R&TC section 18533.
18 (Resp. Opening Br., p. 5 and exhibit I.)

19 On June 28, 2004, appellant submitted a letter to respondent with a formal “request for
20 innocent spouse relief” attached. In a letter dated July 16, 2004, respondent requested information from
21 appellant, including copies of returns, financial information and appellant’s marital status. On July 2,
22 2004, respondent notified appellant’s former spouse of her request for innocent spouse relief. (Resp.
23 Opening Br., p.5.)

24 There is a dispute of fact as to whether appellant submitted the IRS Form 8857 to
25 respondent in September of 1999. Appellant has only provided a copy of the Form 8857 with her appeal
26 but there is not indication from that copy that it was actually filed with respondent. Moreover, appellant
27 has not presented a certified mail receipt or other evidence that the Form 8857 was submitted to
28 respondent.

1 Regardless of whether appellant has presented sufficient evidence to show that she
2 submitted the Form 8857, it appears that the evidence presented may establish that the October 13, 1999,
3 letter was a good faith attempt to request innocent spouse relief and may be considered as such a
4 request.⁵ First, there is no dispute that respondent received appellant's October 13, 1999, letter and that
5 the letter raised the issue as to whether she was eligible for innocent spouse relief under the 1999
6 provisions of R&TC section 18533. Secondly, respondent did not raise the timeliness issue in its
7 correspondence dated September 3, 2003, and July 16, 2004, or in its opening brief to this appeal.
8 Finally, respondent reviewed the matter and issued a Notice of Action for Relief from Joint Tax
9 Liability on January 28, 2005, in which respondent denied appellant's request because she failed to
10 provide "new substantial information" that would entitle her to innocent spouse relief. Thus, there is no
11 indication that respondent ever considered that appellant's October 13, 1999 letter did not constitute a
12 timely request for innocent spouse relief under R&TC section 18533.

13 At the hearing, respondent should be prepared to explain why appellant must demonstrate
14 that she made a timely election for relief in view of the fact that respondent treated the October 13,
15 1999, letter as a timely filed, valid request for relief.

16 Appellant has correctly noted that the two-year statute of limitations is expressed only in
17 subdivision (b), dealing with traditional relief. It is not clear whether the two-year statute of limitations
18 set forth in Revenue Procedure 2003-61, *supra*, applies to subdivision (f) equitable relief under
19 California law. The parties should address that point further at the hearing.

20 **II. Whether R&TC section 18533, subdivision (e)(3)(B), bars the Board from reaching the**
21 **merits of appellant's claim for innocent spouse relief?**

22 ***Contentions***

23 ***Appellant's Contentions***

24 Appellant contends that R&TC section 18533, subdivision (e)(3)(B), does not bar the
25 Board from considering the merits of her request for innocent spouse relief. Appellant emphasizes that
26 the prior appeal set forth different statutory standards for granting innocent spouse relief and that R&TC
27

28 _____
⁵ Appellant's letter appears to staff to be analogous to a timely but insufficient appeal which is later perfected by the appellant. (See Cal. Code of Regs., tit. 18, section 5424.)

1 section 18533 did not include subdivisions (b) and (f) at that time. (App. Supp. Br., pp. 2-3.) Appellant
2 contends that she did not “meaningfully participate” in the prior appeal, which would have precluded the
3 instant appeal under R&TC section 18533, subdivision (e)(3)(B), because this appeal involves issues
4 that are “distinctly different” from the prior appeal. In addition, appellant contends that she was not a
5 meaningful participant because she was not aware of her rights under section 18533 because the
6 applicable provisions were not in existence at the time of the prior hearing. (App. Supp. Br., pp. 4-5.)
7 Thus, appellant contends that the Board’s decision in the prior appeal is not conclusive.

8 ***Respondent’s Contentions***

9 Respondent contends that R&TC section 18533, subdivision (e)(3)(B), bars the Board
10 from considering the merits of appellant’s request for innocent spouse relief. Respondent states that it
11 had concluded from its prior review that the meaning of “participated meaningfully” was unclear and
12 therefore, that appellant should be allowed to demonstrate that she met the definition of an “innocent
13 spouse” pursuant to the current provisions of R&TC section 18533. Respondent further states that its
14 earlier determination was based on the federal regulation interpreting IRC section 6015 and dicta from
15 *Hopkins v. Commissioner* (2003) 120 T.C. 451. Respondent contends *Hopkins* did not address the issue
16 of whether the taxpayer in that case had “participated meaningfully”. However, respondent asserts that
17 three subsequent cases, *Noons v. Commissioner*, T.C. Memo 2004-243 [88 T.C.M. 388], *Huynh v.*
18 *Commissioner*, T.C. Memo 2006-180 and *Lincir v. Commissioner*, T.C. Memo 2007-86, each addressed
19 the issue of meaningful participation and are, therefore, relevant to this appeal. (Resp. Supp. Br., pp. 4-
20 5.)

21 In each of those cases, the court ruled that the taxpayer had participated meaningfully in a
22 prior proceeding within the meaning of IRC section 6015, subdivision (g)(2), the parallel federal
23 statutory provision to R&TC section 18533, subdivision (e)(3)(B). Respondent contends that appellant
24 attended the hearing with a representative and participated in the hearing by responding to inquiries
25 from Board members. Moreover, respondent asserts that the court in *Lincir* found that the taxpayer
26 participated meaningfully even though the more recent innocent spouse provisions of IRC section 6015
27 were not available during the taxpayer’s earlier litigation. Thus, respondent contends that, like the
28 taxpayer in *Lincir, supra*, the fact that the current provisions of current R&TC section 18533 were not in

1 effect at the time of the prior appeal does not mean that the respondent did not participate meaningfully
2 in that proceeding. Respondent therefore contends that the Board's decision in the prior appeal is
3 conclusive in this matter. (Resp. Supp. Br., pp. 5-6.)

4 ***Applicable Law***

5 R&TC section 18533, subdivision (e)(3)(B), states in its entirety:

6 In the case of any election under subdivision (b) or (c), if a decision of the
7 board in any prior proceeding for the same taxable year has become final,
8 that decision shall be conclusive except with respect to the qualification of
9 the individual for relief that was not an issue in that proceeding. The
exception contained in the preceding sentence does not apply if the board
determines that the individual participated meaningfully in the prior
proceeding.

10 From the above-quoted statutory language, it follows that the Board's determination in a prior
11 proceeding controls the outcome in a subsequent proceeding involving the same taxable year unless:
12 (1) the qualifications for relief in the subsequent proceeding were not at issue in the prior proceeding,
13 and (2) the taxpayer did not participate meaningfully in the prior proceeding. (See *Vetrano v.*
14 *Commissioner* (2001) 116 T.C. 272, 278.)

15 The federal counterpart to R&TC section 18533 is IRC section 6015. IRC section 6015
16 is organized similar to R&TC section 18533, containing provisions for traditional relief under
17 subdivision (b), separate-liability relief under subdivision (c), and equitable relief under subdivision (f).
18 In addition, IRC section 6015(g)(2) contains language that is substantially identical to R&TC section
19 18533, subdivision (e)(3)(B), providing for the conclusive effect of prior proceedings.

20 While there is not yet authority interpreting R&TC section 18533, subdivision (e)(3)(B),
21 there is now considerable federal authority interpreting IRC section 6015(g)(2). When a California
22 statute is substantially similar to a federal statute, federal law interpreting the federal statute is generally
23 considered highly persuasive. (*Douglas v. State of California* (1942) 48 Cal.App.2d 835.) In particular,
24 the Board has noted that "federal precedent is applied extensively in California innocent spouse cases."
25 (*Appeal of Patricia Tyler-Griffis supra*, citing Rev. & Tax. Code, § 18533, subd. (g)(2).)

26 The Internal Revenue Service's interpretation of IRC section 6015(g)(2) is set forth in
27 Treasury Regulation 1.6015-1(e), which states in pertinent part:

28 A requesting spouse has not meaningfully participated in a prior
proceeding if, due to the effective date of section 6015, relief under

1 section 6015 was not available in that proceeding. Also, any final
2 decisions rendered by a court of competent jurisdiction regarding issues
3 relevant to section 6015 are conclusive and the requesting spouse may be
collaterally estopped from relitigating those issues.

4 The tax court has held that IRC section 6015(g)(2) applies to claims for equitable relief under
5 subdivision (f). (*Thurner v. Commissioner* (2003) 121 T.C. 43, 51.) This is because a claim for
6 equitable relief is “subordinate and ancillary” to traditional claims for relief under subdivisions (b) and
7 (c). (*Id.*; see also *Appeal of Patricia Tyler-Griffis, supra.*) There was meaningful participation in a prior
8 proceeding where the taxpayer was made aware of her right to elect innocent spouse relief. (*Moore v.*
9 *Commissioner*, T.C. Memo 2007-156.) There was meaningful participation in a prior proceeding where
10 the taxpayer participated in pretrial preparations and testified at trial, even though the prior case only
11 involved the underlying tax liability. (*Huynh v. Commissioner*, T.C. Memo 2006-180.) Where there
12 was meaningful participation in a prior proceeding, the prior proceeding is conclusive even though the
13 more-recently enacted and expanded relief provisions of section 6015 were not available at the time.
14 (*Lincir v. Commissioner*, T.C. memo 2007-86.) Finally, the requesting spouse bears the burden of
15 proving, by a preponderance of the evidence, that she did not participate meaningfully in the prior
16 proceeding. (*Monsour v. Commissioner*, T.C. Memo. 2004-190.)

17 ***Staff Comments***

18 In the present case, the Board has made a determination in a prior proceeding for the
19 same taxable years that appellant is not entitled to innocent spouse relief. Under R&TC section 18533,
20 subdivision (e)(3)(B), the Board’s prior determination is conclusive unless: (1) the qualifications for
21 relief in this appeal are different than the qualifications for relief in the prior appeal, and (2) appellant
22 did not participate meaningfully in the prior proceeding.

23 Appellant contends that the qualifications for relief at issue in this appeal are different
24 from those in the prior appeal because R&TC section 18533 has been substantially amended in the
25 meantime. Staff acknowledges that section 18533, as in effect during appellant’s prior proceeding, was
26 organized quite differently from the current version and did not contain some of the current version’s
27 specific provisions. However, it appears that the qualifications for relief have not been substantially
28 changed. Former section 18533, subdivision (a), required the electing spouse to show that the

1 understatement of tax was attributable to the other spouse, that she did not know of and had no reason to
2 know of the item giving rise to the understatement, and that, taking into account all facts and
3 circumstances, it is inequitable to hold her liable for the deficiency. Those same requirements are
4 contained in the current section 18533, subdivision (b)(1). Furthermore, those elements also are
5 important considerations in granting equitable relief under current section 18533, subdivision (f). (See
6 Rev. Proc. 2003-61, *supra*, § 3.03.) Therefore, it appears the qualifications for relief at issue in this
7 appeal are the same as those at issue in the prior appeal.

8 It is appellant's burden to prove that she did not meaningfully participate in her prior
9 appeal. (*Monsour v. Commissioner, supra.*) Appellant contends that her participation was not
10 meaningful because the current version of R&TC section 18533 contains new avenues for relief that
11 were not available during her prior appeal. However, as discussed above, the elements of relief under
12 current section 18533 appear to be substantially the same as those in former section 18533. Even under
13 Treasury Regulation 1.6015-1(e), upon which appellant relies, a prior decision on issues relevant to
14 relief are conclusive in the subsequent proceeding. It is undisputed that appellant consulted with
15 counsel, appeared at the oral hearing, and testified at the oral hearing during the course of her prior
16 appeal.⁶ It is also undisputed that appellant requested innocent spouse relief in her prior appeal. The tax
17 court has found meaningful participation where the taxpayer had less participation than appellant did in
18 her prior appeal. (E.g., *Moore v. Commissioner, supra; Huynh v. Commissioner, supra.*) It therefore
19 appears that appellant participated meaningfully in her prior appeal.

20 If the Board concludes that the qualifications for relief at issue in this appeal are the same
21 as those at issue in the prior appeal, or that appellant participated meaningfully in the prior appeal, then
22 the Board's prior decision is conclusive in this matter. If the Board concludes that neither of those
23 conditions are satisfied, then it must move on to the final issue and consider appellant's request for
24 innocent spouse relief.

25 ///

26 ///

27 _____

28 ⁶ A copy of the transcript of hearing can be found as exhibit G to respondent's opening brief.

1 **III. Is appellant entitled to innocent spouse relief?**

2 ***Contentions***

3 ***Appellant's Contentions***

4 Appellant contends that she is entitled to innocent spouse relief pursuant to R&TC
5 section 18533, subdivision (b)(1) because she meets the following conditions:

- 6 • Appellant and her spouse filed a joint return.
- 7 • The understatement of tax is attributable to erroneous items of appellant's spouse.
- 8 • Appellant has established that in signing the return she did not know of, or have reason to know
9 of, the understatement.
- 10 • In giving consideration to all of the facts and circumstances, it is inequitable to hold appellant
11 liable for the deficiency for the tax years attributable to the understatement.

12 (Appeal Letter, pp. 4-5.)

13 In an exhibit to the appeal letter dated February 23, 2005, appellant describes her
14 husband's mental breakdown and two suicide attempts in 1990 and her subsequent discovery that he had
15 embezzled from funds that he managed. As a result, she states that she suffered from acute anxiety that
16 required medication and professional attention. She also describes her marriage as a relationship in
17 which she managed domestic matters while her husband, a certified public accountant, handled all of the
18 couple's financial affairs. She states that her background is in education and that she has no business,
19 finance or accounting training. She further states that she only signed the returns in issue because her
20 husband was in the hospital and the returns were delinquent. She only learned about the extent of her
21 husband's embezzlement when formal charges were filed nearly two years later. (Appeal Letter, exhibit
22 D.)

23 Appellant also maintains that respondent has not shown the basis for its determination
24 that payment of the tax liability, then in excess of \$370,000, would not result in a hardship to appellant.
25 Appellant states that she would have paid the liability if she had been able and then filed a claim for
26 refund. She also states that it appears that respondent was aware of her husband's bankruptcy, but chose
27 not to consider that fact in making its determination. (Appeal Letter, p.9.)

28 Appellant subsequently filed an opening brief in which she cites the case of *Cook v.*

1 *Commissioner*, T.C. Memo 2005-22, for the proposition that she could only be held responsible for her
2 actual knowledge of the amount of omitted income and that mere knowledge of the source of omitted
3 income is not sufficient to establish actual knowledge. In addition, appellant maintains that she set forth
4 the reasons for equitable relief in the appeal letter, and that there has been no evidence presented as to
5 her ability to pay the tax and accrued interest liability. (App. Opening Br., pp. 1-2.)

6 On December 5, 2005, appellant filed a reply brief in which she sets forth in greater detail
7 the circumstances which she believes show that she is entitled to innocent spouse relief. First, appellant
8 maintains that the tax liability and accrued interest at that time totaled over \$400,000 which was several
9 times her yearly net earnings. She then makes several points in support of her request in addition to
10 those mentioned above, which include the following summarized here:

- 11 • Appellant is a primary school teacher approaching retirement age.
- 12 • Appellant was unaware of her husband's embezzlement at the time of commission and appellant
13 did not knowingly or materially benefit from the embezzlement.
- 14 • Appellant's husband filed for bankruptcy which caused the liquidation of assets and distribution
15 to husband's creditors.
- 16 • Respondent's audit was conducted while her husband was incarcerated so appellant was not able
17 to verify the audit findings because her husband's records were not available at that time.
- 18 • Appellant was found not to have committed willful or fraudulent acts with respect to the
19 underreporting of income. The absence of a fraud penalty against appellant is evidence that
20 appellant was not involved in the preparation of submission of the tax returns.
- 21 • Respondent grossly exaggerated the amount of her husband's embezzlement as \$1,700,000,
22 which is substantially more than the additional taxable income of \$786,000 determined by
23 respondent.
- 24 • Respondent did not properly allow deductions or adjustments to the underreported income so
25 there is doubt as to respondent's tax liability determination.
- 26 • Appellant was never aware that the embezzled funds were used for the couple's living expenses
27 and they did not take expensive vacations as characterized by respondent.
- 28 • Most of the embezzled money was invested in ill-fated business ventures.

- 1 • Appellant and her husband maintained separate bank accounts and she had no knowledge of
2 funds deposited to and withdrawn from her husband's accounts and his business entities.
- 3 • If appellant had known of the extent of the embezzlement she would have filed a separate return.
- 4 • With respect to real property acquired through sale of the family residence, appellant held the
5 residence in joint tenancy and received her share of the proceeds from the sale in bankruptcy.
6 The sale and purchase were made as appellant's sole and separate property transactions. With
7 respect to the funding of the family trust for Brian, David and Allison Dorfler, the original trustor
8 and trustee was appellant's father and she only became the successor trustee upon his death in
9 2002. Appellant never had an interest in the trust properties.
- 10 • Respondent has attacked appellant's "love and devotion and belief in the marriage vows"
11 because of her husband's criminal acts. Under the law, marital status is not a factor in the
12 innocent spouse relief determination.
- 13 • Appellant's statements are credible and satisfy her burden of proof and respondent has not shown
14 that they are not trustworthy. Any statements by appellant's representative in the prior appeal
15 should not be attributed to appellant.

16 (App. Reply Br., pp. 2-11.)

17 ***Respondent's Contentions***

18 Respondent contends that appellant has not demonstrated that she is entitled to innocent
19 spouse relief because she has not established that in signing the returns for each of the appeal years she
20 did not know of, or have reason to know of the understatement of tax, or that it would be inequitable to
21 hold her liable for the deficiencies. Respondent points out that in the prior hearing, appellant's
22 representative conceded that statements made to appellant prior to signing the 1988 and 1989 returns
23 should have raised questions in her mind that there were income amounts that had not been reported.
24 Respondent asserts that appellant has made bare assertions that contradict her representative's
25 statements but has not presented any supporting evidence. Respondent adds that appellant was highly
26 educated and completely understood that income may not have been reported on the returns.
27 Respondent also asserts that appellant's later financial transactions involving real estate sales and her
28 position as a trustee and party to sale and purchase transactions of real property demonstrates that her

1 level of understanding of financial matters was beyond her representations in this appeal. Finally,
2 respondent contends that the facts do not establish that appellant met the requisite duty of inquiry as to
3 items on a return. (Resp. Opening Br., pp. 8-9.)

4 Respondent also contends that appellant has not shown that “taking into account all facts
5 and circumstances”, it would be inequitable to hold appellant liable for the additional taxes and
6 penalties. In this respect, respondent contends that appellant has not presented any evidence that she
7 would suffer economic hardship or that requiring appellant to pay the liability would be inequitable. In
8 addition, respondent contends that appellant has not presented any evidence that her husband abused her
9 and, even though she may have suffered emotionally, appellant continued to work. Finally, respondent
10 contends that appellant has not shown or alleged that her husband was deceitful or evasive or that he
11 made all the financial decisions. (Resp. Opening Br., p. 9.)

12 With respect to appellant’s request for equitable relief under R&TC section 18533,
13 subdivision (f), respondent asserts that the federal guidelines set forth in Revenue Procedure 2003-61 are
14 applicable. Under those guidelines, respondent maintains that the evidence in the record supports
15 respondent’s determination denying relief. Respondent asserts that appellant has not presented evidence
16 sufficient to meet her burden of proof to show that she satisfied the elements for equitable relief.

17 Respondent cites the following facts:

- 18 • Appellant has only made self-serving statements and has not demonstrated that she did not know
19 or have reason to know of the income understatements.
- 20 • There is no evidence that appellant would suffer economic hardship if relief is not granted and
21 the failure to present such evidence should weigh heavily against appellant.
- 22 • Appellant has a legal obligation to pay the tax liability.
- 23 • Appellant is still married to the spouse with whom she failed to report the 1988, 1989 and 1990
24 income.
- 25 • There is no third party testamentary evidence.

26 Finally, respondent states that it has discretionary authority to grant relief on equitable
27 grounds and respondent’s denial of that relief may be reversed only if the Board finds that respondent
28 abused that discretion. Respondent states that a state agency may be found to have abused its discretion

1 when its finding has no reasonable basis or is not otherwise supported by or contrary to the evidence. An
2 abuse of discretion may also be committed when the agency's finding is arbitrary, capricious or
3 fraudulent. Respondent asserts that appellant has only pointed to respondent's determination to allow
4 her request for relief as evidence that she did not participate in the prior hearing. However, respondent
5 maintains that appellant misconstrues respondent's determination which was that appellant did
6 participate but that it may not have risen to level of meaningful participation. In any event, respondent
7 contends that appellant has not established the elements required for equitable relief so as to show that
8 respondent abused its discretion by denying that request for relief. (Resp. Opening Br., pp. 9-11.)

9 ***Applicable Law***

10 When a husband and wife file a joint return, their tax liability is joint and several and
11 respondent is entitled to assert the entire tax liability against either party. (Rev. & Tax. Code, § 19006,
12 subd. (b).) However, under the innocent spouse provisions of R&TC section 18533, an individual who
13 files a joint return may be relieved of all or a portion of such joint and several liability. The individual
14 claiming innocent spouse relief has the burden of proving that each statutory requirement is satisfied.
15 (*Stevens v. Commissioner* (11th Cir. 1989) 872 F.2d 1499; *Appeal of Frederick and Charlotte Dillett*,
16 85-SBE-012, Feb. 5, 1985.)

17 R&TC section 18533, subdivision (b), sets forth "traditional" innocent spouse relief.
18 Under subdivision (b), an individual can seek relief from liability with respect to an understatement of
19 tax attributable to the erroneous items of the other individual filing the joint return. The electing
20 individual must show that, in signing the return, she did not know of, and had no reason to know of, the
21 understatement of tax, and taking into account all facts and circumstances it is inequitable to hold her
22 liable for the deficiency attributable to that understatement. (Rev. & Tax. Code, § 18533, subd. (b)(1).)
23 The requesting spouse has reason to know of an understatement if a reasonably prudent taxpayer in the
24 electing spouse's position, at the time the return was signed, could be expected to know that the return
25 contained an understatement or that further investigation was warranted. (*Butler v. Commissioner*
26 (2000) 114 T.C. 276, 283-284.) The spouse seeking relief has a "duty of inquiry." (*Id.*) Key factors for
27 consideration include: (1) the electing spouse's education level and involvement in the family's business
28 and financial affairs, (2) the presence of lavish or unusual expenditures as compared to the family's past

1 income levels, income standards, and spending patterns, and (3) the culpable spouse’s evasiveness and
2 deceit concerning the couple’s finances. (*Id.*) Even if appellant did not fully review the joint return
3 before signing it, she may be charged with knowledge of its contents. (*Hayman v. Commissioner*
4 (2nd Cir. 1993) 992 F.2d 1256, 1262; *Terzian v. Commissioner* (1979) 72 T.C. 1164, 1170.)

5 Regarding whether it is equitable to hold the electing spouse liable for the tax, material
6 factors include whether there has been a significant benefit to the electing spouse beyond normal
7 support, and whether the failure to report the correct tax liability results from concealment,
8 overreaching, or any other wrongdoing on the part of the nonelecting party. (*Jonson v. Commissioner*
9 (2002) 118 T.C. 106.) Essentially the same language appears in the equities test of R&TC section
10 18533, subdivision (b)(1)(D), providing for “traditional” innocent spouse relief, and R&TC section
11 18533, subdivision (f), providing for “equitable” innocent spouse relief (see discussion, *infra*), and the
12 equitable factors considered are the same. Thus, the same conclusion as to whether it is equitable to
13 hold a party claiming relief liable would conceivably flow from either provision. (*Alt v. Commissioner*
14 (2002) 119 T.C. 306, 316; *Butler v. Commissioner, supra*, at p. 291.)

15 R&TC section 18533, subdivision (f), gives respondent the discretion to provide
16 “equitable” innocent spouse relief from “any unpaid tax or any deficiency (or any portion of either),”
17 when a taxpayer does not qualify for innocent spouse relief under R&TC section 18533,
18 subdivisions (b) and (c). When a request for equitable relief is coupled with a request for traditional
19 relief (as it is here), the Board generally has jurisdiction to determine if respondent’s failure to grant
20 equitable innocent spouse relief amounts to an abuse of discretion. (Rev. & Tax. Code, § 18533,
21 subd. (e)(1)(A); *Appeal of Patricia Tyler-Griffis, supra.*) Respondent’s denial of equitable relief is
22 entitled to considerable deference unless it is arbitrary, capricious, or without sound basis in fact.
23 (*Jonson v. Commissioner, supra; Pacific First Federal Savings Bank v. Commissioner* (1993) 101 T.C.
24 117.)

25 In Revenue Procedure 2003-61, the IRS set forth a non-exhaustive list of factors that are
26 relevant to equitable relief. As relevant to this appeal, that list includes:

- 27 • Economic hardship – whether the requesting spouse would suffer economic
28 hardship if relief is not granted;

- 1 • Knowledge or reason to know – in a deficiency case, whether the requesting
- 2 spouse knew or should have known of the item giving rise to the deficiency; and
- 3 • Significant benefit – whether the requesting spouse received a significant benefit
- 4 from the item giving rise to the deficiency.

5 (See Rev. Proc. 2003-61, *supra*, § 4.03(2)(a).)

6 ***Facts, Contentions, and Comments***

7 Staff has attached the hearing summary for appellant’s prior appeal as exhibit A.

8 Because the facts surrounding the underreporting of income have not changed and the essential elements
9 for innocent spouse relief are the same as they were 11 years ago, staff incorporates the facts and
10 arguments set forth in the prior hearing summary. In addition, the transcript of the prior oral hearing is
11 attached to respondent’s opening brief as exhibit G.

12 With respect to her request for traditional relief under subdivision (b), appellant should be
13 prepared to show that, at the time she signed the returns, she did not know of, and could not know of, the
14 underreported income. (*Butler v. Commissioner, supra.*) When she signed the returns, appellant had a
15 duty of inquiry. (*Id.*) Staff notes that appellant signed a 1988 return reporting only about one-quarter of
16 the couple’s income, and she signed a 1989 return reporting only about one-tenth of the couple’s
17 income. Staff further notes that appellant signed those returns after she learned of the embezzled
18 money. Appellant must show that, nevertheless, she reasonably believed the returns to be correct.

19 With respect to her request for equitable relief under subdivision (f), appellant should be
20 prepared to show that respondent’s denial of relief was arbitrary and capricious. (*Jonson v.*
21 *Commissioner, supra.*) Appellant also must show that she did not know of the embezzled income; that
22 she received no significant benefit from the embezzled income, and that she would suffer economic
23 hardship if required to pay the liability. (See Rev. Proc. 2003-61, *supra.*) The facts as presented in the
24 attached hearing summary from the prior hearing appear to make it difficult for appellant to show the
25 first two of those three factors. For example, it appears undisputed that appellant did, in fact, know of
26 the embezzled income when she signed the returns. It also appears that the embezzled income was used
27 to maintain appellant’s living standards and pay for appellant’s vacations to Europe and Hawaii.

28 If the Board reaches the merits of the innocent spouse issue, appellant should be prepared

1 to address staff's concerns, which are expressed above.

2 Attachments: Exhibits A and B

3 ///

4 ///

5 ///

6 Dorfler_la

7

8

9

10

11

12

13

14

15

16

17

18

19

20

21

22

23

24

25

26

27

28

EXHIBIT A

CALIFORNIA STATE BOARD OF EQUALIZATION

PERSONAL INCOME TAX APPEAL**HEARING SUMMARY**

<u>Appellant</u>	<u>Years</u>	<u>Proposed Assessments</u>
Rochelle Dorfler	1988	\$11,867
95A-0991	1989	61,066
	1990	120

Representing the Parties:

For Appellant: Rochelle Dorfler
For Franchise Tax Board: Mark McEvelly, Counsel

Counsel for Board of Equalization: Jeffrey G. Angeja, Tax Counsel

QUESTION: Whether appellant has established that she is entitled to relief of tax liabilities as an innocent spouse.

Appellant filed joint California personal income tax returns with Elliott L. Dorfler, appellant's husband, for the 1988, 1989, and 1990 tax years. The 1988 and 1989 returns were signed on November 20, 1990, while the 1990 return was signed on October 15, 1991. During the period of February 1986 through September 1990, appellant's husband, a certified public accountant, was employed as a managing director of California Contemporary, Inc. (CCI). In that capacity, he was in charge of and had control over accounting records and bank accounts for CCI, as well as an estate and various trusts. On June 29, 1992, appellant's husband pled guilty to charges of embezzlement in the theft of over \$1.7 million from these entities and was sentenced to three years in prison.

In 1993, respondent began an audit examination of appellant and her husband. As a result of the examination, on June 9, 1994, respondent issued Notices of Proposed Assessment (NPA's) for each of the appeal years. The NPA's increased the taxable income reported by appellant and her husband by the amounts respondent determined had been embezzled. The 1988 NPA proposed increased income of \$136,475 and additional tax of \$11,867; the 1989 NPA proposed increased income of \$657,476 and additional tax of \$61,066; and the 1990 NPA proposed increased income of \$3,000 and additional tax of \$120. Each of the NPA's proposed the assessment of a fraud penalty.⁷

Appellant protested the NPA's, maintaining that she was an innocent spouse. After considering appellant's protest, respondent determined that she did not qualify for innocent spouse relief. Consequently, on June 26, 1995, respondent issued a Notice of Action for each of the appeal years which affirmed its determinations. This timely appeal followed.

Where a husband and wife file a joint return, the liability for the tax on their income is joint and several. (Rev. & Tax. Code, § 18555, subd. (b); Appeal of Donald Morris, Cal. St. Bd. of

⁷During appellant's protest, respondent determined that these fraud penalties should not apply to appellant since the fraud was related solely to the activities of her husband.

1 Equal., June 30, 1980.) Thus, it is within respondent's discretion to assert the whole tax against either
2 spouse. (Appeal of Donald Morris, supra.) Nevertheless, a spouse who files a joint return will be
3 relieved of liability for the tax arising from an erroneous deduction if: (1) the understatement is
4 attributable to the other spouse; (2) the innocent spouse did not know of or have reason to know of the
5 understatement; and (3) it is inequitable to hold the innocent spouse liable for the tax, taking into
6 account all of the facts and circumstances, including whether the spouse benefited significantly from the
7 understatement. (Rev. & Tax. Code, § 18402.9, renumbered to § 18533, operative Jan. 1, 1994; Appeal
8 of Juan F. and Elizabeth M. Lopez, Cal. St. Bd. of Equal., May 4, 1983; Appeal of Frederick and
9 Charlotte Dillett, Cal. St. Bd. of Equal., Feb. 5, 1985.) The spouse claiming entitlement to innocent
10 spouse relief has the burden of establishing each statutory requirement. (Stevens v. Commissioner (11th
11 Cir. 1989) 872 F.2d 1499; Appeal of Frederick and Charlotte Dillett, supra.)⁸

12 Appellant asserts that she has no accounting or bookkeeping background, and therefore
13 left all financial matters, including the preparing and filing of tax returns, to her husband. Appellant
14 says she signed and filed the tax returns for the appeal years on the advice of counsel. In addition,
15 appellant states that her husband placed all of the embezzled funds in his various business investments,
16 and that all such funds were eventually lost. Finally, appellant contends that she had no actual
17 knowledge of her husband's activities prior to signing and filing the tax returns for the appeal years,
18 although appellant admits that she signed and filed such returns after learning that her husband had
19 embezzled funds during those years.

20 Respondent contends that appellant has failed to satisfy any of the foregoing criteria.
21 First, respondent argues that the understatement of income is not solely attributable to appellant's
22 husband, because appellant signed and filed joint returns which failed to report the embezzled funds
23 after she learned of her husband's embezzlement.

24 Next, respondent asserts that appellant had constructive knowledge of the understatement
25 and/or reason to know of it because she signed and filed the tax returns, which included very little of her
26 husband's income, after she learned of his embezzlement. (See Price v. Commissioner (9th Cir. 1989)
27 887 F.2d 959; Weiss v. Commissioner (1990) ¶90,492 T.C.M. (P.H.).) In support of this contention,
28 respondent states that innocent spouse relief has been denied where there were sufficient facts within the
taxpayer's knowledge at the time of signing a return to provide a reasonably prudent taxpayer with
reason to know of the omitted embezzlement income, i.e., discharge from employment, criminal
indictment, or criminal conviction for embezzlement, citing Trimmer v. Commissioner (1983) ¶83,131
T.C.M. (P.H.).

Finally, respondent contends that appellant has failed to demonstrate that she did not
benefit directly or indirectly from the understatement of income or that it would be inequitable to hold
her liable for the deficiency. Respondent relies upon statements from the district attorney's investigative
report that appellant's husband had stated to three separate people that the embezzled funds had been
used for the maintenance of the living standards for he and appellant. Respondent also references a
statement from that report which indicates that trips to Europe and Hawaii were realized from the
embezzled funds. Based on the foregoing, respondent requests that its determinations be sustained.

At the hearing, staff requests that the parties address each of the innocent spouse
requirements in light of the standards announced by the court in Pietromonaco v. Commissioner (9th
Cir. 1993) 3 F.3d 1342. In addition, staff requests the parties to address whether the IRS granted
innocent spouse relief to appellant for the appeal years.

⁸Former Revenue and Taxation Code section 18402.9, renumbered to section 18533, operative January 1, 1994, is similar to
Internal Revenue Code section 6013(e), and therefore federal interpretations are highly persuasive as to the proper application
of the California sections. (Meanly v. McColgan (1942) 49 Cal.App.2d 203.)

EXHIBIT B

October 11, 1996

Mr. James S. Hurwitz
1592 Union Street, #90
San Francisco, California 94123

Dear Mr. Hurwitz:

Appeal of Rochelle Dorfler
95A-0991

<u>Years</u>	<u>Proposed Assessments</u>
1988	\$11,867
1989	61,066
1990	120

This is to inform you that on October 10, 1996, at the conclusion of its calendar of hearings, the Board of Equalization considered the above-entitled appeal, and concluded that appellant had not established that she was entitled to innocent spouse relief. Therefore, the Board ordered that the action of the Franchise Tax Board on appellant's protest against the proposed assessments of personal income tax in the amounts and for the years set forth above be sustained.

This decision will become final 30 days from the date of the Board's decision unless, within that time, you or the Franchise Tax Board file a petition for rehearing with this Board requesting reconsideration of this Board's decision and clearly stating the reasons for the request. If you file a petition for rehearing, you should send one copy to the Board of Equalization and one copy to the Franchise Tax Board.

Sincerely,

Jeffrey G. Angeja
Tax Counsel

cc: Franchise Tax Board

Final\ltr-decis\dorfler.ja