CALIFORNIA LAWYERS ASSOCIATION
TAXATION SECTION
TAX PROCEDURE & LITIGATION COMMITTEE
MAY 2018

EXTEND THE STATUTE OF LIMITATIONS FOR CLAIMING INNOCENT SPOUSE RELIEF FOR §6015(b) AND §6015(c), MAKING ALL §6015 FORMS OF RELIEF CO-TERMINUS WITH THE §6502 COLLECTION STATUTE.

CLARIFY AND CODIFY THE STANDARD AND SCOPE OF JUDICIAL REVIEW OF §6015(b), §6015(c) and §6015(f).

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EXECUTIVE SUMMARY

Internal Revenue Code Section 6015 allows a requesting spouse who filed a joint income tax return to obtain relief from joint and several liability for a deficiency of tax when the erroneous item giving rise to the deficiency is properly attributable only to the non-requesting spouse. This paper recommends two amendments to §6015, each enhancing fairness and increased access to the benefits Congress intended for qualifying requesting spouses.[2] Neither proposal would change the stringent requirements to qualify for §6015 relief based on the facts and circumstances of the requesting spouse.

The first amendment would extend the statute of limitations for seeking relief pursuant to §6015(b) (traditional relief) and §6015(c) (allocated relief) to be co-terminus with the §6502 period for collecting an assessment. Equitable relief pursuant to §6015(f) may be requested through the end of the §6502 collection period; this change would make the period to request relief pursuant to §6015 the same for all three forms of relief.

The second amendment would codify the standard and scope of Tax Court review of equitable requests for §6015 relief. The proposed amendment would require a de novo review based on the administrative record established at the time of the determination and any additional evidence. This change would make the standard and scope of review the same for §6015(b), §6015(c) and §6015(f).

Extending the period to request relief pursuant to §6015(b) and §6015(c).

Internal Revenue Code Section 6015 allows a taxpayer who filed a joint income tax return to obtain relief from joint and several liability for a deficiency of tax in three situations. This relief is commonly referred to as innocent spouse relief. For two of those situations, §6015(b) and §6015(c), a spouse must elect relief within two years from the date Internal Revenue Service (IRS) collection efforts commence. The statute does not expressly state the period within which relief may be sought in the third situation (§6015(f), equitable relief); however, by Notice 2011-70, the IRS announced that the period within which relief may be elected under §6015(f) extends to the close of the period during which the IRS may collect the tax; that is, at least ten years. A truncated period to request relief under two of the three §6015 subsections is at odds with the character of the statute, which is to make the benefits of §6015 relief available to taxpayers who qualify on the merits of their facts and circumstances. This proposal recommends a simple amendment to §6015, so that the period for requesting relief is the same for §6015(b), (c) and (f).

[2] Both proposed amendments relate to the Taxpayer First Act (HR 5444) pending before Congress, which was passed by the House of Representatives on April 18, 2018 by a vote of 414 to 0.

A person claiming relief as an innocent spouse under §6015(b), §6015(c) or §6015(f) should be allowed to elect relief at any time during which the IRS has authority to collect the tax underpayment. The longer statute of limitations acknowledges the complexities of marital relations. It is consistent with the spirit of Congressional intent to provide relief from joint and several liability to all qualifying requesting spouses to whom erroneous tax items are attributed solely on the grounds of a jointly filed tax return, or for whom responsibility for a joint liability would be inequitable.

Enforcement of the two-year period for seeking relief under §6015(b) and §6015(c) can result in unduly harsh consequences for taxpayers who are entitled to relief but do not seek relief within the statutory two-year period. This is especially true where the spouses do not divorce or become legally separated until after the two-year period, or begin living in separate households more than one year after collection activity begins. In addition, *pro se* taxpayers – the vast majority of taxpayers who might qualify for relief – likely find the two-year statute a trap for the unknowing and unwary. The earliest statutory versions of relief from joint and several liability for innocent spouses did not include a two-year limitation on the request period. Inexplicably, the two-year period was included with other, more beneficially expansive revisions to innocent spouse relief with the enactment of §6015 in 1998.

Enactment of this simple statutory amendment will bring consistency and increased fairness to the foundational element of the statute; i.e., the period for requesting relief. All other existing requirements to qualify for relief remain the same. The amendment will make relief pursuant to §6015(b) and §6015(c) available to the taxpayers whom these separate forms of relief were intended to benefit, and whose requests are rejected because the two-year application period closed and they cannot qualify for equitable relief pursuant to §6015(f). The change will not increase stress on the IRS or the Tax Court, which have been administering and deciding §6015 matters for decades.

This amendment will ensure certainty pertaining to the statute of limitations, in contrast to continued use of Revenue Procedures and Notices to modify the statute's implementation. Most important, the change will allow the IRS to focus on collecting unpaid liabilities from the person whose actions created the liability and who, under §6015, should be accountable for satisfying the liability.

<u>Clarifying the standard and scope of judicial review of §6015(b), §6015(c) and §6015(f)</u>.

The standard and scope of judicial review of requests for relief pursuant to §6015(b), §6015(c) and §6015(f) should be de novo, based on the administrative record at the time of the determination and any additional evidence. The Taxpayer First Act pending in Congress addresses only §6015(f), and would limit

the record to be considered by the courts to the administrative record at the time of the determination to deny relief plus any newly discovered evidence or evidence that was previously unavailable. In essence, this would codify the "record rule" for §6015(f) equitable relief cases. The Taxpayer First Act provides the opportunity to codify a full de novo judicial review for §6015 cases under all three forms of relief. Currently, courts apply a de novo standard to §6015 cases.

The limitation on the scope of review would be disastrous for requesting spouses, the vast majority of whom are unrepresented. All §6015 cases are fact-intensive. Requesting spouses have no access to discovery or any type of compulsory process prior to petitioning Tax Court or other judicial review – even if the taxpayer had the knowledge or wherewithal to develop a meaningful evidentiary record. In addition, the administrative record often is incomplete or riddled with errors. The courts have allowed a trial de novo for §6015 cases, permitting parties to present evidence outside the administrative record. Often, requesting spouses in Tax Court receive assistance with developing evidence from Low Income Tax Clinics or Tax Court Day of the Docket pro bono attorneys – well after the IRS determination to deny relief. It would work to the material disadvantage of persons seeking innocent spouse relief to circumscribe the evidence the courts may consider when deciding §6015 cases.

These two proposed amendments reinforce Congress's intent to make §6015 relief from joint and several liability available for all qualifying requesting spouses. The rigorous requirements to qualify for relief pursuant to each §6015 subsection would remain unchanged. The IRS and the courts are well-equipped to review all three avenues for relief without additional strain on resources. The IRS and the courts have decades of experience administering and deciding §6015 matters. Each amendment has a natural home in the Taxpayer First Act section 11303 pending before Congress.

DISCUSSION

I. BACKGROUND

A. Joint Income Tax Returns.

Since the Revenue Act of 1918[3] married couples have had the option of filing either joint or separate income tax returns. The same rates applied to both joint and separate returns. A married couple in a community property state could split their income by filing separate returns. In non-community property states, a married couple that filed separate returns would each report his or her separate income. A married couple in a community property state thus could pay a lower tax rate on their income than a similar couple in a non-community property tax state.

During the 1930s and 1940s, several bills were proposed in Congress to place married couples in community property states on the same footing as married couples in non-community property states. These bills focused on two alternate solutions: a) having married couples in community property states who file separate returns report only the income he or she earned or controlled, and b) requiring all married couples to file joint returns.[4] Since there was little benefit in filing a joint return, most married couples filed separate returns.

The Revenue Act of 1948 addressed the problem, and simplified tax reporting for households, by introducing "income splitting." A married couple filing a joint return would compute the tax on half of their taxable income and then double the tax.[5] In this way a married couple in a non-community property state that filed a joint return would pay the same tax on their income as a married couple in a community property state that filed separate returns. The Revenue Act of 1948 also provided advantages to married couples in community property states: For the first time their separate income could also be split and taxed at a lower rate.[6] Since enactment of these provisions, joint returns have been the filing method of choice for married couples.

B. Innocent Spouse Relief Before 1998.

The joint return provisions of the Revenue Act of 1918 and its successors have provided that "the tax shall be computed on the aggregate income, and the liability with respect to the tax shall be joint and several."[7] This

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[3] 40 Stat. 1057, sec. 223.
[4] Spenser Williams, "Joint Income Tax Returns under the Revenue Act of 1948," 36 *Cal. L. Rev.* 289.
[5] Pub. L. No. 41, 67th Cong., 1st Sess., Title III, Husband and Wife, Part I.
[6] *See*, Williams, "Joint Income Tax Returns under the Revenue Act of 1948," 36 *Cal. L. Rev*. 289.
[7] 26 U.S.C. §6023(d)(3).

meant that both spouses were responsible for payment of the entire liability for a joint return year, whether the liability was for a tax shown due on the return, plus penalties and interest, or a deficiency in tax, plus penalties and interest.

Following the enactment of the income splitting provisions of the Revenue Act of 1948 and the successor provisions contained in §6013 of the Internal Revenue Code,[8] joint returns became the preferred method for married couples. As a result, it became clear that the joint and several liability feature could lead to inequitable results, especially where one spouse was responsible for an underreporting of tax on the original return.

To address the inequities resulting from holding one spouse liable for a deficiency attributable to the actions of the other spouse, in 1971, Congress enacted the first innocent spouse provision as section 1 of P.L. 91-679, which added subsection (e) to §6013. This provision permitted relief from joint and several liability if a spouse claiming relief could prove:

- The couple's joint return omitted from gross income an amount in excess of 25% of the gross income reported on the return;
- The amount omitted was attributable to the other spouse;
- At the time the joint return was filed, the requesting spouse neither knew nor had reason to know of the omission;
- Taking into account all of the facts and circumstances, it was inequitable to hold the spouse claiming relief liable for the deficiency in tax for that year; and
- The liability from which relief was sought was attributable to the omission.

The effective date of the innocent spouse provisions contained in subsection (e) was set out in section 3 of P.L. 91-679, which provided:

> The amendments made by the first two sections of this Act shall apply to all taxable years to which the Internal Revenue Code of 1954 applies. Corresponding provisions shall be deemed to be included in the Internal Revenue Code of 1939 and shall apply to all taxable years to which such Code applies. Upon application by a taxpayer, the Secretary of the Treasury shall redetermine the liability for tax (including interest, penalties, and other amounts) of such taxpayer for taxable years beginning after December 31, 1961, and ending before January 13, 1971. The preceding sentence shall apply solely to a taxpayer to whom the application of the provisions of section 6013(e) of the Internal Revenue Code of 1954, as added by this Act, for such taxable years is prevented by the operation of res judicata, and such redetermination shall be made without regard to such rule of law. Any overpayment of tax

[8] All references to Code sections are to the Internal Revenue Code unless otherwise specified.

> by such taxpayer for such taxable years resulting from the redetermination made under this Act shall be refunded to such taxpayer.

The Treasury Regulation promulgated under the 1971 version of §6013(e) stated that relief was not available for "a tax deficiency resulting from erroneous or fraudulent deductions, claims or other evasions or avoidances of tax."[9] The regulation further provided that relief was not available for any taxable year if a claim for credit or refund was barred.[10]

Congress expanded the scope of innocent spouse relief in 1984 to allow relief where a deficiency was attributable to omitted income, erroneous deductions, credits or basis in property of the other spouse. As amended §6013(e) provided:

> (e) Spouse relieved of liability in certain cases.
> (1) In general. Under regulations prescribed by the Secretary, if—
> (A) a joint return has been made under this section for a taxable year,
> (B) on such return there is a substantial understatement of tax attributable to grossly erroneous items of one spouse,
> (C) the other spouse establishes that in signing the return he or she did not know, and had no reason to know, that there was such substantial understatement, and
> (D) taking into account all the facts and circumstances, it is inequitable to hold the other spouse liable for the deficiency in tax for such taxable year attributable to such substantial understatement, then the other spouse shall be relieved of liability for tax (including interest, penalties, and other amounts) for such taxable year to the extent such liability is attributable to such substantial understatement.
> (2) Grossly erroneous items. For purposes of this subsection, the term 'grossly erroneous items' means, with respect to any spouse—
> (A) any item of gross income attributable to such spouse which is omitted from gross income, and
> (B) any claim of a deduction, credit, or basis by such spouse in an amount for which there is no basis in fact or law.
> (3) Substantial understatement. For purposes of this subsection, the term 'substantial understatement' means any understatement (as defined in section 6662(d)(2)(A)) which exceeds $500.
> (4) Understatement must exceed specified percentage of spouse's income.

[9] §1.6013-5(d), Income Tax Reg., T.D. 7320 (1974).
[10] §1.6013-5(e), Income Tax Reg., T.D. 7320 (1974).

(A) Adjusted gross income of $20,000 or less. If the spouse's adjusted gross income for the preadjustment year is $20,000 or less, this subsection shall apply only if the liability described in paragraph (1) is greater than 10 percent of such adjusted gross income.
(B) Adjusted gross income of more than $20,000. If the spouse's adjusted gross income for the preadjustment year is more than $20,000, subparagraph (A) shall be applied by substituting '25 percent' for '10 percent'.
(C) Preadjustment year. For purposes of this paragraph, the term 'preadjustment year' means the most recent taxable year of the spouse ending before the date the deficiency notice is mailed.
(D) Computation of spouse's adjusted gross income. If the spouse is married to another spouse at the close of the preadjustment year, the spouse's adjusted gross income shall include the income of the new spouse (whether or not they file a joint return).
(E) Exception for omissions from gross income. This paragraph shall not apply to any liability attributable to the omission of an item from gross income.
(5) Special rule for community property income. For purposes of this subsection, the determination of the spouse to whom items of gross income (other than gross income from property) are attributable shall be made without regard to community property laws.

Neither the 1971 nor the 1984 version of innocent spouse relief contained any time limits for seeking relief.[11] The only limitation was that contained in §1.6013-5(e), Income Tax Reg., which made relief unavailable for taxable years for which a claim for credit or refund was barred. There were no reported decisions interpreting this regulation and no revenue rulings or procedures requiring that a claim for relief be filed within a specified time.

C. Congress Acts to Expand §6015/Innocent Spouse Relief.

On July 30, 1997, President Clinton signed into law the Taxpayer Bill of Rights 2 ("TBOR2").[12] Section 104 of TBOR2[13] directed the Treasury Department and the Comptroller General to conduct separate studies and report to Congress on:

[11] See, National Taxpayer Advocate, *Unlimit Innocent Spouse Relief,* at p. 5, available online at https://taxpayeradvocate.irs.gov/Media/Default/Documents/ResearchStudies/arc10_vol2_unlimit_innocent_spouse.pdf
[12] Pub. L. 104-168, 110 Stat. 1452.
[13] 110 Stat. 1459.

> (1) the effects of changing the liability for tax on a joint return from being joint and several to being proportionate to the tax attributable to each spouse,
> (2) the effects of providing that, if a divorce decree allocates liability for tax on a joint return filed before the divorce, the Secretary may collect such liability only in accordance with the decree,
> (3) whether those provisions of the Internal Revenue Code of 1986 intended to provide relief to innocent spouses provide meaningful relief in all cases where such relief is appropriate, and
> (4) the effect of providing that community income (as defined in section 66(d) of such Code) which, in accordance with the rules contained in section 879(a) of such Code, would be treated as the income of one spouse is exempt from a levy for failure to pay any tax imposed by subtitle A by the other spouse for a taxable year ending before their marriage.

On October 21, 1997, the first version of H.R. 2627, the IRS Restructuring and Reform Act, was introduced in the House of Representatives.[14] Section 321 of the bill provided for the enactment of a new §6015 of the Code to provide for innocent spouse relief for a spouse similar to that provided under §6013(e): It was available to a spouse who established that a) the requesting spouse did not know or have reason to know of the understatement, and b) it would be inequitable to hold the requesting spouse liable for the underpayment. The bill contained three major changes to then-existing law: a) It required the requesting spouse to claim relief within two years of the assessment of the deficiency, b) it required the IRS to develop a special form for claiming relief, and c) it allowed a person whose request was denied to petition the Tax Court. H.R. 2627 went through several iterations in the House with no major change to the proposed §6015.[15]

It was not until February 1998, after H.R. 2627 was referred to the Senate, that Treasury and the General Accounting Office ("GAO") reported to Congress on their separate studies of innocent spouse relief.[16] The Assistant Secretary of Treasury for Tax Policy and the Director, Tax Policy & Administration Issues, of GAO testified about their respective agency's reports before the Oversight Subcommittee of the House Ways and Means Committee on

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[14] See https://www.congress.gov/bill/105th-congress/house-bill/2676/text/ih?.

[15] The innocent spouse provisions in the House versions of the bill and the version referred to the Senate were as reported in the House on October 31, 1997, https://www.congress.gov/bill/105th-congress/house-bill/2676/text/rfs?, as engrossed in the House on November 5, 1997, https://www.congress.gov/bill/105th-congress/house-bill/2676/text/eh?, and as reported in the Senate on November 5, 1997, https://www.congress.gov/bill/105th-congress/house-bill/2676/text/rfs?.

[16] The GAO report is available at https://www.gao.gov/archive/1998/gg98072t.pdf. Treasury's report is available at https://www.treasury.gov/resource-center/tax-policy/Documents/Report-Joint-Liability-Innocent-Spouse-1998.pdf.

February 24, 1998.[17] The reports recommended loosening the standards for obtaining innocent spouse relief, giving a taxpayer the right to Tax Court review of a failure to grant relief and staying collection action while a taxpayer sought relief. Neither in the reports nor testimony did Treasury or GAO recommend limiting the time period for seeking innocent spouse relief.

The Senate version of the bill altered the House amendments to innocent spouse relief. First, it included a right to request that a deficiency be allocated among the joint-filing taxpayers when the spouses are divorced, legally separated or no longer living together. The bill required that a spouse seeking such relief request it within two years after the IRS began collection activities. Second, it provided for equitable relief when other forms of innocent spouse relief were not available.[18] The bill as engrossed in the Senate contained identical provisions.

The bill that emerged from the Congressional conference retained the House bill's expansion of the circumstances under which a taxpayer could obtain innocent spouse relief as well as the Senate amendments relating to taxpayers who are divorced, legally separated or no longer living together. In addition, the Conference legislation authorized the IRS "to provide equitable relief in appropriate situations."[19] The Conference Report stated that the bill as agreed to in conference provided an election period which did "not expire until two years after the first collection activity taken by the IRS after the date of enactment." Neither the Conference Report nor the earlier reports on the House and Senate versions of the bill stated the reason for a two-year election period.[20]

D. Current §6015/Innocent Spouse Provisions.

The IRS Restructuring and Reform Act of 1998 ("the 1998 Reform Act") was signed into law on July 22, 1998. The 1998 Reform Act repealed the innocent spouse provisions of former §6013(e) and added the new §6015, which was effective for liabilities that arose after July 22, 1998, or that arose on or before July 22, 1998 but remained unpaid as of that date.[21]

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[17] A transcript of the hearing is available at https://www.gpo.gov/fdsys/pkg/CHRG-105hhrg60950/html/CHRG-105hhrg60950.htm.

[18] The bill reported in the Senate is available at https://www.congress.gov/bill/105th-congress/house-bill/2676/text/rs?. The Senate version of the bill did not contain any provisions relating to "traditional" innocent spouse relief; i.e., §6015(b).

[19] Conf. Rep. No. 559, 105th Cong., 2nd Sess. 249-255 (1998), available online at https://www.congress.gov/congressional-record/1998/06/24/house-section/article/H5100-1?.

[20] *Ibid.* See, also, H.Rep. 105-364 (Oct. 31, 1997), available at https://www.congress.gov/congressional-report/105th-congress/house-report/364/1, and S. Rep. 105-174 (April 22, 1998). Although the Senate Report states that a taxpayer would have two years after the first collection action to request relief, it does not state the reason for the limitation.

[21] 1998 IRS Reform Act sec. 3201(g)(1).

Section 6015 allows innocent spouse relief via three sets of procedural rules for seeking relief, each in a different circumstance, frequently referred to as avenues for relief.

The first circumstance, set out in **§6015(b)**, is available to all taxpayers who filed a joint return in which there is an understatement of tax attributable to erroneous items of the other spouse. A spouse requesting relief (the requesting spouse) is relieved of liability for tax (plus any penalties and interest thereon) attributable to an understatement if the requesting spouse establishes that:

- a joint income tax return was filed for the year for which relief is sought;
- the return contains an understatement of tax attributable to erroneous items of the other spouse (the non-requesting spouse);
- in signing the return, the requesting spouse did not know and had no reason to know of such understatement;
- taking into account all of the facts and circumstances it would be inequitable to hold the requesting spouse liable for the deficiency in tax attributable to such understatement; and
- the requesting spouse requests relief no later than two years after the Secretary has begun collection activities with respect to the requesting spouse.[22]

The second circumstance, **§6015(c)**, is available to a requesting spouse who: a) is no longer married to the non-requesting spouse; or b) is legally separated from the non-requesting spouse; or c) has not been a member of the same household as the non-requesting spouse at any time during the twelve months immediately preceding the date upon which innocent spouse relief is requested.[23] If §6015(c) relief is granted, the liability is limited to the portion of any deficiency allocated to the requesting spouse.[24] The requesting spouse has the burden of proving the portion of the deficiency attributable to him or her.[25]

A spouse may not limit liability to any portion of a deficiency due to an erroneous item if the Secretary can prove that, at the time the requesting spouse signed the return, he or she had actual knowledge of the erroneous item.[26] For instances when omitted income gave rise to the erroneous item, knowledge of the item includes knowledge of the receipt of the income.[27] In cases of erroneous deductions, including credits, knowledge of the item means knowledge of the facts that made the item not allowable as a deduction or credit.[28]

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[22] §6015(b)(1).
[23] §6015(c)(3)(A)(1).
[24] *Ibid.*
[25] §6015(c)(2).
[26] §6015(c)(3)(C).
[27] §1.6015-3(c)(2)(A), Income Tax Reg.
[28] §1.6015-3(c)(2)(B), Income Tax Reg.

A taxpayer who seeks to limit liability under §6015(c) must request relief within two years after the date on which the Secretary has begun collection activity against him or her.[29]

When §6015(c) relief is granted, the liability is computed for the requesting spouse as if a separate tax return was filed, subject to specific rules. The non-requesting spouse remains legally responsible for the entire liability. If both spouses elect relief under the allocation rules, they both remain jointly and severally liable for any portion of the liability not allocable to either spouse under the rules contained in §6015(d).[30]

The third avenue to §6015 relief applies when equitable relief is warranted, under **§6015(f)**. The Secretary may relieve a taxpayer of liability pursuant to §6015(f) when relief is not available under §6015(b) or (c). Relief is available for both deficiencies in tax and underpayments of tax reported on a joint income tax return. Congress delegated to the Secretary the duty to promulgate rules for obtaining equitable relief. Section 6015 does not impose a time limit for seeking equitable relief under subsection (f).[31]

E. The Enlargement of the Time Period for Seeking Equitable Relief under §6015(f).

To claim innocent spouse relief under §6015(b), (c) or (f), a taxpayer must file a request using IRS Form 8857. The IRS originally maintained that a request for equitable relief under §6015(f) had to be filed within two years of the IRS's first collection activity against the requesting spouse. The IRS promulgated §1.6015-5, Income Tax Reg., which provided that to "elect the application of §1.6015-2 or §1.6015-3, or to request equitable relief under §1.6015-4, a requesting spouse must file Form 8857 or other similar statement with the Internal Revenue Service no later than two years from the date of the first collection activity against the requesting spouse after July 22, 1998, with respect to the joint tax liability."

Taxpayers whose claims for equitable relief were denied on the basis that the request was filed more than two years after the first collection activity challenged the application of the two-year time limit in a series of court cases. In several cases, the Tax Court held that the regulation imposing a two-

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[29] § 6015(c)(3)(B).

[30] §1.6015-3(d)(1)(ii), Income Tax. Reg.

[31] The Taxpayer First Act, H.R. 5444, passed by the House of Representatives on April 18, 2018 and currently pending in the Senate, would codify the period for requesting relief pursuant to §6015(f). Section 11303 of the proposed legislation, entitled Clarification of Equitable Relief From Joint Liability, would permit taxpayers to request relief pursuant to §6015(f) for tax that has not been paid any time before the expiration of "the applicable period of limitation under §6502 [that is, the period for collection after assessment] or, for tax that has been paid, any time during the period in which the individual could submit a timely claim for refund or credit of such payment." The Taxpayer First Act does not address §6015(b) or (c).

year time period for seeking equitable relief was an invalid interpretation of the statue. In three cases that were appealed, the appellate courts reversed the Tax Court, holding that under *Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc.,*[32] the regulation was a reasonable interpretation of an ambiguous statue. *Lantz v. Commissioner*,[33] *Mannella v. Commissioner*,[34] *Jones v. Commissioner*.[35]

On July 25, 2011, shortly after the Fourth Circuit's opinion in *Jones*, the IRS issued Notice 2011-70. The Notice provided that the IRS would consider requests for equitable relief under §6015(f) if the period of limitation on collection of taxes provided by §6502 (i.e., Collection after Assessment) remains open for the tax years at issue. If the relief sought involves a refund of tax, then the period of limitation on credits or refunds provided in §6511 (i.e., the limitations on credit or refund) will govern whether the IRS will consider the request for relief for purposes of determining whether a credit or refund may be available. The Notice further provided that taxpayers seeking equitable relief could rely on it until promulgation of final regulations modifying the two-year rule or other guidance was issued.

The Secretary issued Prop. Reg. §1.6015-5 on August 13, 2013.[36] Among other things, the proposed regulation would amend §1.6015-5(b)(1), Income Tax Reg., to apply only to applications for relief under §6015(b) or (c), and would add §1.6015-5(b)(2), Income Tax Reg., to provide that applications for equitable relief could be filed at any time while the period of limitations on collection remains open. In addition, claims for credit or refund could be filed within the time periods provided in §6511. The regulation has not become final.

II. THE HARSH EFFECTS OF THE §6015(b) AND §6015(c) TIME LIMIT TO REQUEST RELIEF.

A. The Time Limits for Requesting Relief under §6015(b) and §6015(c) Work a Hardship on Taxpayers Who Are Otherwise Eligible for the Statute's Beneficial Effect.

The current two-year time limit for seeking relief under §6015(b) and §6015(c) can work a hardship on taxpayers who are otherwise eligible for relief. Consider the following examples:[37]

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[32] 467 U.S. 837 (1984).
[33] 607 F.3rd 479 (7th Cir. 2010), *rev'g* 132 T.C. 131 (2009).
[34] 631 F.3rd 115 (3rd Cir. 2011*), rev'g* 132 T.C. 196 (2009).
[35] 642 F.3rd 459 (4th Cir. 2011).
[36] Fed. Reg. vol. 78, No. 156, p. 49242.
[37] Note that these examples, for purposes of this proposal, presume that the requesting spouse would satisfy the other §6015 requirements and are denied relief primarily due to the application of the truncated §6015(b) and §6015(c) statute of limitations for requesting relief from joint and several liability.

Example 1. Sally and Ed are married and have two young children. Sally has a successful business as an architect who operates a business as a single member limited liability company. Ed is a partner in a small local accounting firm. Neither spouse is involved in the other's business. The IRS assesses a deficiency of $500,000 based on improper deductions taken by Sally's LLC. Ed applies for innocent spouse relief under §6015(b) within two years of the IRS beginning collection activities. His request is denied because one of the accountants in his firm prepared Sally's books and records and their joint return; therefore, according to the IRS, Ed should have known about the improper deductions. Facts show, however, that Ed did not have actual knowledge of the erroneous items attributable solely to Sally. Ed did not know Sally's deductions were improper; he did not know the facts that made the deductions improper. In point of fact, the accountant who prepared the income tax return for Sally's company did not know the deductions were improper. Return preparers are permitted to rely on the representations of their clients when accepting information for tax returns. In Sally's case, the accountant had no reason to question the information she provided pertaining to the return.

Eighteen months after collection activity commences, Sally and Ed separate and establish separate households. Ed applies for innocent spouse relief under §6015(c), which may be granted if the requesting spouse did not have actual knowledge of the erroneous item. In this example, the two-year statute of limitations to request relief dooms Ed's eligibility. If Ed submits the Form 8857 request within the two-year period, his request will be denied as premature, since he has not been living in a separate household for at least one year. If he files after the one-year period, his request will be denied as late. Because Ed has separate assets and income sufficient to pay the liability and the IRS determines he should have known of the underreporting, he is denied §6015 equitable relief, even though the erroneous item was Sally's. Under the two-year statute, Ed's error was not separating from Sally sooner – solely for the purpose of obtaining relief for which he is otherwise eligible under §6015(c).

Example 2. A deficiency is assessed against Ed and Sally due to Ed's failure to report all of the income from his business. Because they have a daughter in college and do not have any marital problems at the time the return was filed, Ed and Sally do not separate or institute divorce proceedings. Ed tells Sally that he will take care of the unpaid tax but does not, which leads to friction between them. After their daughter graduates from college, Sally files a petition for dissolution of marriage. A final decree of dissolution is entered by the state court more than a year after the petition is filed. Sally then requests innocent spouse relief under §6015(c). Because the Form 8857 application is filed more than two years after collection action began, it is untimely. She is denied relief under §6015(c). Due to her financial situation, Sally is denied equitable relief under §6015(f) even though the erroneous item undisputedly is Ed's.

Example 3. Liam owns a construction company. His wife Emma is a high school teacher whose parents have left her assets in a trust. Liam developed a gambling addiction, as a result of which he began siphoning money from his construction business. Between 2009 and 2011, he skimmed over $600,000, most of which he used for gambling. He was able to hide his gambling from his wife. In 2012 the IRS began an audit of the tax returns of Liam and his company for 2009 and 2010. The auditor expanded the audit to include 2011. The audit was handled by Liam's accountant, who was able to resolve the case with the agent by agreeing to a deficiency of tax of $210,000, an accuracy penalty and interest. The deficiency was assessed in 2013. Liam tells Emma the tax bill is due to bookkeeping errors by his staff and that he will make arrangements to take care of payment. She accepts his explanation. After an offer in compromise to reduce the liability (that is, an OIC application) is rejected, Liam and Emma sign an installment payment agreement with the IRS.

Liam makes payments for the first thirteen months. Due to his gambling, he defaults on the agreement. It is only after the IRS levies their joint bank account that Liam tells Emma the truth – that he has a gambling problem and stopped making the IRS installment payments. It is now more than two years after the IRS's first collection activity. But for the fact that more than two years have passed, Emma would be eligible for relief under 6015(b). Because she is still married and living with Liam, who has entered counseling, and has assets sufficient to pay the liability, she will not be able to receive §6015(c) relief or §6015(f) equitable relief from a liability entirely attributable to Liam.

B. The Collateral Consequences of the Truncated Statute of Limitations to Request Relief Pursuant to §6015(b) and §6015(c) Are Unintentionally Harsh and Disengaged from the Beneficial Intent of the Law.

The unintentional adverse collateral consequences of the truncated statute of limitations to request relief pursuant to §6015(b) and §6015(c) have emerged as the law has been applied. Inadvertently, the two-year statute to request relief under §6015(c) has become a government-fostered incentive to end marriages for those taxpayers who sought representation early enough to learn of their options in time to satisfy the requirements to be divorced, legally separated or living separate and apart for at least twelve months. Understandably, it is awkward for tax counsel to advise clients that a law exists to grant relief from a liability for a requesting spouse – if and only if the requesting spouse separates from or divorces the non-requesting spouse to whom a liability is rightly allocated.

It is important to note that §6015(f) equitable relief is not a safety net for requesting spouses after the §6015(b) and §6015(c) door shuts. Like §6015(b) and §6015(c), equitable relief under §6015(f) serves its own legal purpose, which does not include liberally granting relief to requesting spouses

who could qualify for traditional or allocated relief but for missing the two-year request period. In fact, §6015(f) expressly is intended to apply when the requesting spouse fails to qualify based on the merits of §6015(b) and §6015(c). The examples above illustrate only a few circumstances when §6015(f) would not offer a safe harbor to requesting spouses who would qualify for traditional or allocated relief.

In addition, §6015(f) as applied by well-intentioned and under-trained IRS professionals fails to serve requesting spouses. The Service simply gets the analysis wrong. As recent examples, two applications for relief were rejected by the IRS Innocent Spouse unit because the requesting spouses failed to establish they suffered abuse. There is no basis in any of the guidance provided by the IRS or the courts to apply a requirement of abuse in order to be granted equitable relief. To the contrary, Revenue Procedure 2013-24 setting forth IRS guidance describing factors to be considered when determining eligibility for §6015(f) relief *expanded* the factual parameters pertaining to physical and emotional abuse to make relief more available in such circumstances. Unrepresented taxpayers confronted with incorrect administrative rejections may not have the wherewithal to rebut these determinations, including undertaking the next – potentially remedial but perhaps seemingly overwhelming – step of petitioning for Tax Court review.

As another collateral consequence, if the Government brought an action to reduce the assessments to judgment against any of these couples, the taxpayer who would have been eligible for innocent spouse relief but for the two-year statute of limitations would be unable to defend against the judgment based upon having qualified as an innocent spouse. *United States v. Haag*.[38]

As the Seventh Circuit noted in *Lantz*, statutes of limitation are arbitrary, because many of the criteria for granting relief under §6015(f) are the same as criteria for granting relief under §6015(b) and §6015(c), "if there is no deadline in subsection (f), the two-year deadlines in subsections (b) and (c) will be set largely at naught because the substantive criteria of those sections are virtually the same as those of (f)."[39] Because there are, however, additional §6015(f) criteria in the form of guidance from a Revenue Procedure,[40] this is not always the case. As a result, many taxpayers who filed joint returns and would otherwise be eligible for relief under §6015(b) or §6015(c) cannot obtain relief

[38] 2004 WL 2650274, 94 AFTR 2d 2004-6665 (D. Mass. Sept. 30, 2004), holding that a wife could not claim innocent spouse status in a suit to reduce an assessment to judgment where she had not filed a request for innocent spouse relief within two years of the IRS's first collection action.

[39] *Lantz v. Commissioner*, 607 F.3d 479, 484 (7th Cir. 2010).

[40] Revenue Procedure 2013-34 provides guidance for a requesting spouse seeking equitable relief from income tax liability under §6015(f). Equitable relief always has been guided by Revenue Procedure with an evolving list of factors to be considered. Applications of the Revenue Procedures has led to independent request analyses, and inconsistent determinations. In particular, *pro se* taxpayers suffer from this situation, and may be the subject of another Delegation proposal.

because of the limiting two-year period for claiming relief. And in those cases when the Government sues to collect an unpaid deficiency, a taxpayer otherwise eligible for relief is prevented from defending on that ground because of the two-year bar.

III. THE STANDARD AND SCOPE OF JUDICIAL REVIEW FOR ALL §6015 FORMS OF RELIEF SHOULD BE DE NOVO, BASED ON THE ADMINISTRATIVE RECORD AND ALL ADDITIONAL EVIDENCE.

Sec. 11303(a)(1) of the Taxpayer First Act would materially limit the scope of judicial review in innocent spouse cases.

The Service's position has been that the Tax Court's review should be limited to the administrative record. This has been rejected both by the Tax Court[41] and the courts of appeal, which have held that the Tax Court is to review the administrative record and any other evidence presented by the parties[42]. The Taxpayer First Act §11303(a)(1) provides that the Tax Court's de novo review would be limited to the administrative record plus any newly discovered or previously unavailable evidence.

The limitation on the scope of review would be disastrous for taxpayers seeking innocent spouse relief, the vast majority of whom are not represented. Form 8857, the request for innocent spouse relief, contains a list of questions with check the box answers and a space for the taxpayer to provide additional information. In part due to budget cuts that have reduced the Service's workforce and impaired training, the review afforded by the Centralized Innocent Spouse Unit is often cursory. Appeals review of a denial of relief is not much better. Appeals attempts to limit the taxpayer to a short telephone call. None of this is conducive to taxpayers creating a complete record for judicial review unless the taxpayer has competent representation.

The limitation on evidence outside the administrative record to that which is newly discovered or was not previously available is similar to one of the grounds for altering or amending a judgment under Fed. R. Civ. Pro. Rule 60(b), which allows a court to alter or amend a judgment based on "newly discovered evidence that, with reasonable diligence, could not have been discovered in time to move for a new trial." The courts have formulated different tests for determining whether evidence is newly discovered, but all require a showing that the evidence existed at the time of the trial, that the person seeking relief could

[41] *Ewing v. Commissioner*, 122 T.C. 32 (2004).
[42] *Wilson v. Commissioner*, 705 F. 3d 980 (9th Cir. 2013), *Commissioner v Neal*, 557 F. 3d 1262 (11th Cir. 2009).

not have discovered or learned of it despite her due diligence and that the evidence would likely have changed the result.[43]

Applying a standard used after a trial in a case where the parties typically are represented by counsel, having the full panoply of discovery and the availability of compulsory process to obtain evidence, to a situation where the party seeking relief is generally unrepresented at the administrative level and had no access to discovery or any type of compulsory process is harsh. The Tax Court and courts of appeal have recognized this in allowing the parties to present evidence outside the administrative record and have had no problem with a rule that allows trial de novo in innocent spouse cases.

Another problem is that the administrative record is often incomplete or riddled with errors. Practitioners recount instances involving innocent spouse and collection due process cases at both the administrative and judicial level when the administrative record either misinterpreted or failed to include statements made during discussions with appeals. Unfortunately, there are instances when the administrative record contains outright misstatements about what happened at appeals.

For all of these reasons, it would work to the disadvantage of persons seeking innocent spouse relief to circumscribe the evidence that courts can consider. Courts with jurisdiction to decide §6015 requests for relief should be permitted to consider the administrative record and all available evidence.

IV. CONCLUSION: PROPOSED STATUTORY CHANGES

Two simple changes to §6015 will bring consistency and increased fairness to the §6015 regimen affording relief from joint and several liability arising from an erroneous item attributable to another spouse, or for equitable reasons. The proposed language is drafted to be naturally accommodated by the Taxpayer First Act.

Section 6015 proposed language for §11303 of the Taxpayer First Act:

Amend the Taxpayer First Act section 11303(a)(1) to provide

(a) In General -- Section 6015 is amended—

(1) in subsection (e), by adding at the end the following new paragraph:

[43] *See*, *Webb v. Exxon*, 856 F.3d 1150, 1159-60 (8th Cir. 2017), *United States v. IBTU*, 247 F.3d 370 (2nd Cir. 2001), *Jones v. Aero/Chem Corp*., 921 F. 2d 875, 878 (9th Cir. 1980).

"(7) STANDARD AND SCOPE OF REVIEW.—Any review of a determination made under this section shall be reviewed de novo by the Tax Court and shall be based upon—

"(A) the administrative record established at the time of the determination, and

"(B) any additional evidence."

Amend the Taxpayer First Act §11303(a)(2) to provide:

(2) the following subparagraphs of § 6015 shall be deleted:

- Delete subparagraph (E) from §6015(b)(1).
- Delete subparagraph (B) from §6015(c)(3).

and following subsection (f) the following new subsection (g) shall be added:

(g) Limitation – Request for Relief. — A taxpayer requesting relief under this subsection shall request such relief from the Secretary (in such form as the Secretary may prescribe) with respect to any portion of any liability that –

(A) has not been paid, provided that such request is made before the expiration of the applicable period of limitation under section 6502 – Collection After Assessment, or

(B) has been paid, provided that such request is made during the period in which the individual could submit a timely claim for refund or credit of such payment.

And current subsection (g) shall be renumbered as subsection (h).