

13-1572

TAX TYPE: INCOME TAX

TAX YEAR: 2008

DATE SIGNED: 9-23-2014

COMMISSIONERS: B. JOHNSON, M. CRAGUN, R. PERO

EXCUSED: D. DIXON

GUIDING DECISION

BEFORE THE UTAH STATE TAX COMMISSION

TAXPAYER-1 AND
TAXPAYER-2,

Petitioners,

vs.

AUDITING DIVISION AND
TAXPAYER SERVICES DIVISION OF THE
UTAH STATE TAX COMMISSION,

Respondents.

**FINDINGS OF FACT, CONCLUSIONS
OF LAW, AND FINAL DECISION**

Appeal No. 13-1572

Account No. #####

Tax Type: Income Tax

Tax Year: 2008

Judge: Phan

Presiding:

Bruce Johnson, Commission Chair

Jane Phan, Administrative Law Judge

Appearances:

For Petitioner: TAXPAYER-1, By Telephone

TAXPAYER-2, By Telephone

For Respondent: REPRESENTATIVE FOR RESPONDENT, Assistant Attorney General

RESPONDENT-1, Taxpayer Services Division

RESPONDENT-2, Auditing Division

STATEMENT OF THE CASE

This matter came before the Utah State Tax Commission for a Formal Hearing on May 20, 2014, in accordance with Utah Code §59-1-501 and §63G-4-201 et seq. Based upon the evidence and testimony presented at the hearing, the Tax Commission hereby makes its:

FINDINGS OF FACT

1. Respondent (“Division”) had issued a Notice of Deficiency and Audit Change jointly against Petitioners (“Taxpayers”) for the 2008 tax year assessing additional Utah individual income tax and interest. The Taxpayers had filed a joint Utah return for the 2008 tax year and the audit was issued against them jointly. Taxpayers appealed the notice and the matter proceeded to the Formal Hearing.

2. The notice was issued on May 30, 2013.¹ The Division had increased the Utah Individual Income tax based on an increase made by the Internal Revenue Service on the Taxpayers' joint federal return. The IRS had increased the Federal Adjusted Gross income from \$\$\$\$\$ to \$\$\$\$\$. This change resulted in a change in Utah individual income tax owed in the amount of \$\$\$\$\$. Interest as of the date of the Notice was \$\$\$\$\$, for a total as of the Notice date of \$\$\$\$\$. Interest continues to accrue on the unpaid balance.

3. The Taxpayers did not challenge or provide evidence that the amount of tax owed as indicated in the audit notice was in error. The challenge to the audit from TAXPAYER-1 was that the Tax Commission should collect the amount from TAXPAYER-2. TAXPAYER-2 did not dispute the amount but stated that she was unable to pay.

4. The Utah return filed by the Taxpayers for the 2008 tax year was a joint return filed as part-year residents. The Taxpayers had been married in 2008, were living together and sharing household expenses.

5. The increased tax amount was the result of unreported income in the amount of \$\$\$\$\$. It appeared to the Division that this amount related to wages from BUSINESS of CITY, for which TAXPAYER-2 had been employed during 2008. There was no information from the Taxpayers to refute this conclusion.

6. Because of the unreported income the Taxpayers' federal return indicated a refund of all withholding and credits in the amount of \$\$\$\$\$. After the IRS recalculated the tax amount to include the unreported income the Taxpayers had a federal tax refund of \$\$\$\$\$. However, instead of the refund being paid to the Taxpayers it was taken to repay a non-IRS debt, a delinquent student loan. The student loan was debt incurred solely by TAXPAYER-2.

7. The Taxpayers divorced in 2010. TAXPAYER-1 provided a copy of their Divorce Decree which indicated that TAXPAYER-2 was responsible to pay the outstanding balance on the 2008 income taxes.² TAXPAYER-2 did not dispute that this was part of the Divorce Decree.

8. The IRS had granted TAXPAYER-1 "Injured Spouse Relief" regarding the federal 2008 payment of the refund to TAXPAYER-2'S student loan. The IRS issued a letter dated November 14, 2013,³ in which it stated, "We have determined that the injured spouse's portion of the overpayment on your joint income tax return is \$\$\$\$\$."

9. Regarding the Utah 2008 audit deficiency, the Taxpayer Services Division considered whether to grant TAXPAYER-1 Innocent Spouse Relief on the Utah taxes. Respondent Taxpayer

¹ Respondent's Exhibit 2.

² Petitioner's Exhibit 1, pg. 8.

³ Respondent's Exhibit 3.

Services Division denied the relief by letter dated March 6, 2014.⁴ In the letter the Division points out that the Divorce Decree is enforceable against only the parties identified in the decree and is not binding to creditors. The Taxpayer Services Division goes on to indicate that the IRS had not granted TAXPAYER-1 Innocent Spouse Relief. At the hearing and its briefing the representative for the Respondents pointed out that there is a difference between “Injured Spouse Relief” and “Innocent Spouse Relief” as determined by the IRS.

10. RESPONDENT-2, Income Tax Audit Manger, for the Auditing Division testified at the hearing regarding the IRS Account Transcript for TAXPAYER-1.⁵ It was his conclusion upon review of the transcript that the IRS had, in fact, included the unreported income in a joint income calculation and assessed tax against both Taxpayers. He explained that the Taxpayers’ original return had indicated a federal refund of \$\$\$\$\$. After the IRS discovered the unreported income there would still have been a refund, but at a lower amount of \$\$\$\$\$. The full amount of the refund had been paid over to TAXPAYER-2’S delinquent student loan. After the “Injured Spouse” claim, the IRS refunded to TAXPAYER-1 roughly one-half of the revised refund which had been taken from him and used to pay TAXPAYER-2’S student loan.

11. The Taxpayer Services Division indicates that it generally will only allow an equitable innocent spouse relief if the IRS has granted innocent spouse relief.

APPLICABLE LAW

Utah Code § 59-1-1417 (2012) provides that the burden of proof is upon the petitioner (the taxpayer) in income tax matters before the Commission, as follows:

In a proceeding before the commission, the burden of proof is on the petitioner except for determining the following . . . [The statute then provides three exceptions; none of which apply to this case.]

Utah Code § 59-10-503(1) (2008-2009) states in relevant part:

. . . .

- (b) If the federal income tax liability of husband or wife is determined on a separate return for federal income tax purposes, the income tax liability of each spouse shall be determined on a separate return under this chapter.
- (c) If the federal income tax liabilities of husband and wife, other than a husband and wife described in Subsection (b), are determined on a joint federal return, they shall file a joint return under this chapter and their tax liability shall be joint and several.

⁴ Respondent’s Exhibit 1.

⁵ Respondent’s Exhibit 4.

CONCLUSIONS OF LAW

1. When spouses file a joint Utah return for a tax year, each spouse is jointly and severally liable for any Utah tax liability. The Utah State Tax Commission may collect the full amount of the audit liability from either spouse under Utah Code Sec. 59-10-503.

2. A Divorce Decree between two spouses indicating which spouse will pay taxes is not binding on the Utah State Tax Commission and does not supersede Utah Code Sec. 59-10-503. Regardless of the decree the Utah State Tax Commission may collect from one or the other spouse or both. Generally, as noted by the Divisions in their Prehearing Brief, “a decree only binds the spouses by an order of the Court, not creditors,” citing *Gardner v Gardner*, 2012 UT App. 374.⁶

3. There is no Utah statutory provision that provides innocent spouse relief specifically. The Utah State Tax Commission may allow such relief under general equitable provisions but has limited this to situations where the IRS has granted “Innocent Spouse Relief.” In this matter TAXPAYER-1 was not granted “Innocent Spouse Relief” from the IRS. He was allowed Injured Spouse Relief and refunded ½ of the joint federal tax refund that had been taken and paid over to a debt owed solely by TAXPAYER-2. From IRS records it appears that the IRS did tax both Taxpayers jointly on the unreported income and did not provide relief to TAXPAYER-1 on the tax amount owed. Further, although the determination would need to be made by the IRS, it does not appear that TAXPAYER-1 would have met the IRS criteria for “Innocent Spouse Relief” which is set out at IRS Code Sec. 6015(b). Some of the IRS requirements are that there was a substantial understatement of tax attributable to grossly erroneous items of one spouse, the innocent spouse shows lack of knowledge and it would be unfair to hold the innocent spouse liable. In this situation it was not shown that TAXPAYER-1 was unaware TAXPAYER-2 was employed and earning wages from the BUSINESS of CITY and the two shared in the household expenses, so he would have benefited from the income. The lack of knowledge or unfairness criteria has not been shown. Additionally, the mistake on the part of the Taxpayers does not seem to rise to the level of a substantial understatement of tax attributable to grossly erroneous items of one spouse.

The audit deficiency against the Taxpayers for the 2008 tax year should be upheld and the Taxpayer Service Division not limited to collect this amount solely from TAXPAYER-2.

Jane Phan
Administrative Law Judge

⁶ Respondent’s Prehearing Brief, Pgs. 2-3.

DECISION AND ORDER

Based on the foregoing, the Commission denies the Taxpayers' appeal. The audit deficiency is sustained and the amount may be collected based on joint and several liabilities against either Taxpayer. It is so ordered.

DATED this _____ day of _____, 2014.

R. Bruce Johnson
Commission Chair

D'Arcy Dixon Pignanelli
Commissioner

Michael J. Cragun
Commissioner

Robert P. Pero
Commissioner

Notice of Appeal Rights: You have twenty (20) days after the date of this order to file a Request for Reconsideration with the Tax Commission Appeals Unit pursuant to Utah Code Ann. §63G-4-302. A Request for Reconsideration must allege newly discovered evidence or a mistake of law or fact. If you do not file a Request for Reconsideration with the Commission, this order constitutes final agency action. You have thirty (30) days after the date of this order to pursue judicial review of this order in accordance with Utah Code Ann. §59-1-601 et seq. and §63G-4-401 et seq.