Franchise Tax Board

ANALYSIS OF AMENDED BILL

Author:	Haynes	Analyst:	LuAnna Hass	Bill Number:	SB 366
Related Bills:	See Legislative History	Telephone:	845-7478	Amended Date:	May 1, 2001
		Attorney:	Patrick Kusiak	Sponsor:	

SUBJECT: Taxpayer Bill of Rights/No Levy May be Made on Principal Residence of Innocent Partner/Release of Certain State Tax Liens

SUMMARY

Under this bill, the Franchise Tax Board (FTB) would be:

- prohibited from seizing and selling (levying) a principal residence of an innocent partner if the reason for the levy is the fraudulent action of another partner.
- required to release any state tax liens on or the proceeds from the sale of the principal residence of an innocent partner if the innocence of the owner is substantiated.
- prohibited from extending any state tax lien beyond the authorized ten-year period.
- prohibited from allowing a state tax lien to attach to a taxpayer's property that qualifies as a "declared homestead."

SUMMARY OF AMENDMENTS

The May 1, 2001, amendments would prevent a state tax lien from attaching to a taxpayer's property that qualifies as a "declared homestead" and prohibit FTB from extending tax liens.

The April 16, 2001, amendments would require a state tax lien to be released on an escrow or other account holding the proceeds from the sale of an innocent partner's principal residence. The amendments also would remove the term "limited" in reference to innocent partners.

This is the department's first analysis of this bill.

PURPOSE OF THE BILL

According to the author's office, the purpose of this bill would be to offer an innocent investor in a fraudulent partnership protection from losing their home.

EFFECTIVE/OPERATIVE DATE

This bill would be effective and operative on January 1, 2002.

POSITION

Pending.

Board Position:			Department Director	Date
_____ S	_____ NA	_____ NP		
_____ SA	_____ O	_____ NAR	Alan Hunter for GHG	06/20/01
_____ N	_____ OUA	___X___ PENDING		

Summary of Suggested Amendments

At the author's request, amendments are provided to address the department's implementation concerns and selected policy concerns.

ANALYSIS

FEDERAL/STATE LAW

A sole proprietorship, corporation, and partnership are three primary forms in which a business is commonly conducted. California recognizes four forms of partnerships, which include joint ventures: general partnerships, limited partnerships, limited liability partnerships, and limited liability companies, which can be classified as a partnership for tax purposes. A partnership in general is an entity in which two or more persons join together to carry on a trade or business. Each partner contributes money, property, labor, or special skills, and each expects to share in the profits and losses from the business activity.

For tax purposes, partnerships file information-type returns rather than income tax returns because partnerships pass through their income, losses, credits, and gains to their partners. The amount of the partner's distributive share of income, losses, credits, or gains is generally based on the partner's interest in the partnership. The partners include their distributive share of income, losses, credits, and gains on their tax return to compute their tax liability. In the case of a partnership loss, that loss will reduce the partner/taxpayer's taxable income and, hence, reduce the taxpayer's tax liability. In many cases, the loss offsets (shelters) the taxpayer's other income items. Partnerships may claim substantial losses that lack economic substance, and the partners in turn will reflect these losses on their own returns. The losses can be substantially larger than the amount of the partner's actual economic investment in the partnership. A partnership is considered to be an abusive tax shelter if fraudulent statements are made regarding the receipt of various tax benefits, including credits, deductions, or income that could be excluded from taxation. A gross valuation overstatement also is a consideration in the determination of an abusive tax shelter.

For FTB to determine whether income, losses, credits, or gains are correctly claimed on a tax return, FTB uses various information sources, including Internal Revenue Service (IRS) audits. When the partner is a California resident, the IRS notifies FTB of the revenue agent's report (RAR) that contains the federal audit results.

Upon receipt of the RAR, FTB will then review the taxpayer's California tax return, the basis for the federal audit adjustment, and propose any appropriate California tax deficiency assessments. Penalties are assessed, as appropriate[1]. Interest accrues on proposed tax deficiency assessments from the original due date of the tax return on which tax should have been reported.

If payment in full is not made, FTB notifies the taxpayer that collection action may commence. If the taxpayer is experiencing financial hardship, the taxpayer may make installment payments or defer payment. If the taxpayer does not have the income, assets, or ability to pay the amount due in the foreseeable future, the taxpayer may make an offer, and the department may accept a lesser amount (called an "Offer-in-Compromise" (OIC)). An OIC is processed on a case-by-case basis. Once the amount offered and accepted is paid, the case is closed, and any state tax liens are released.

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[1] In the case of abusive tax shelters, FTB generally will assess fraud penalties against only the promoters or owners of the abusive tax shelter and not those individuals who are merely investors.

Levies

Under state and federal tax law (including several laws identified as Taxpayers' Bill of Rights (TBR)), before a taxpayer's property can be levied by either FTB or IRS to pay an amount due, the taxpayer must be provided a notice of intent to levy and an opportunity to request a review of the intended action. Further, the state and federal TBRs require each taxing authority to consider whether the action to levy the taxpayer's property balances the need for the collection of the tax with the concern that the collection action is no more intrusive than necessary. Additionally, FTB is required to release any lien on property where the expense of the sale process would exceed the amount due.

State and federal laws also provide that the taxpayer's principal residence cannot be levied by either FTB or IRS to pay an amount due, if the amount due is $5,000 or less. If the amount due exceeds $5,000, then in order to levy a taxpayer's residence:

- FTB must obtain a court order and the taxpayer would likely be allowed the homestead exemption (described below), which is generally available to most judgment debtors under the Code of Civil Procedure.

- IRS must obtain approval from the court.

While the department is reluctant to seize and sell a taxpayer's residence, levying a personal residence is considered on a case-by-case basis if the circumstances warrant such a measure.

Liens

Under current law, an enforceable tax lien is automatically created when a taxpayer fails to pay an amount that becomes due and payable. To be generally recognized and to compete with non-tax liens, a notice of state tax lien must be recorded in the county where real property is located and attach to a taxpayer's interest in all real property owned by the taxpayer in that county. Once recorded, real property will be subject to that state tax lien for 10 years, unless released earlier by FTB or extended. The extension of a state tax lien is considered on a case-by-case basis. At the time the taxpayer sells or refinances real property, an escrow company will record documents and disburse funds relating to the transaction. Through the escrow, any money that would otherwise be paid to the seller is used to clear liens from the title to the property, including state tax liens. The amount of the state tax lien generally must be paid in full to be released by FTB. A state tax lien attaches to any dwelling notwithstanding the prior recording of a homestead declaration, as described below.

Current state tax law allows FTB to release all or any portion of the property subject to a lien if the department determines that the taxes are sufficiently secured by a lien on other property, or that the release will not endanger or jeopardize the collection of taxes.

Homestead Declaration/Homestead Exemption

Current law allows individuals to declare that a particular property is the principal dwelling of that person or that person's spouse. The declaration must be recorded in the county where the property is located. In general, if the homestead declaration is recorded prior to a judgment lien, the judgment lien does not attach to the property, except to its value in excess of the homestead exemption.

If exercised, the homestead exemption will protect a portion of an individual's equity in the property in the event a judgment creditor forces the sale of that property to satisfy a judgment debt. In the event of such a sale, an amount equal to the homestead exemption would be paid to the individual from the proceeds of the sale before any money is paid to the creditor. The value of a homestead exemption ranges from $50,000 to $125,000 depending upon the individual's marital status, age, income, or health.

Bankruptcy

Federal law outlines the procedures for voluntary and involuntary bankruptcy proceedings. The most common, Chapter 7 bankruptcy, provides that a trustee may be appointed to liquidate the assets (estate) of the debtor (taxpayer). Federal bankruptcy laws exempt certain properties from liquidation and may apply to a debtor's primary residence.

While a debtor is in bankruptcy, they are protected by the automatic stay, which requires creditors to cease all active collection action. Generally, the automatic stay is effective from the date the debtor files for bankruptcy protection until the case is either discharged or dismissed.

Exempt property is not liable during or after a bankruptcy proceeding for taxpayer debts that were incurred prior to the bankruptcy, unless the debt is secured by a properly filed tax lien. Therefore, the state tax lien continues to attach to any pre-bankruptcy real property of the taxpayer that exists in the county where the lien was recorded. The department will collect through its recorded state tax lien the outstanding tax debt when the taxpayer voluntarily sells or refinances the residence. The department will satisfy the lien by collecting any amount available to cover the tax debt prior to the taxpayer receiving the homestead exemption amount.

<u>THIS BILL</u>

Under this bill, FTB:

- could not levy a principal residence of an innocent partner if the reason for the levy is the fraudulent action of another partner.

- would be required to release state tax liens on the principal residence of an innocent partner if the innocence of the owner is substantiated. The lien release would also apply to escrow accounts in which the proceeds are from the sale of a principal residence of an innocent partner.

- would be unable to extend a state tax lien beyond the initial ten-year period.

An "innocent partner" would mean any partner in a partnership, limited partnership, or joint venture, who:

1. did not engage in any fraudulent action that resulted in an underpayment of tax to which the lien relates, and

2. was not aware of any fraudulent action that resulted in an underpayment of tax to which the lien relates.

An “innocent partner” would include a spouse or former spouse of any “innocent” partner, in a partnership, limited partnership, or joint venture.

This bill would specify that any tax lien filed with a county recorder does not constitute a lien against the “declared homestead” of the taxpayer, unless a penalty for fraud has been assessed against the taxpayer.

IMPLEMENTATION CONSIDERATIONS

Staff has identified several implementation considerations. The attached amendments would resolve these concerns, as discussed with the author’s office.

1. The bill, as amended, provides that liens *may* rather than *shall* not take affect during bankruptcy. Changing “shall” to “may” places FTB in violation of the bankruptcy laws. Amendment 2 reverses the change. Amendment 4 incorporates by reference the requirement that liens be released in bankruptcy cases for these innocent investors, which is the author’s intent.

2. According to the author’s office, this bill is intended to protect individuals like those characterized in various newspaper articles as investors in partnerships promoted by Walter J. Hoyt III. As detailed under “Program Background,” Hoyt was convicted of various criminal acts involving fraudulent activity. However, the criminal acts that were not classified as fraud may have been the actions that resulted in the investor’s tax adjustments and underpayment. Therefore, this bill may not grant these investors the relief intended by the author. The attached Amendment 4 redefines the “innocent” person in relationship to investors in abusive tax shelters, which was the case of the “Hoyt” investors.

3. As amended, the bill would require the department to release liens on proceeds from the sale of an innocent partner’s principal residence in escrow. An escrow period, which typically lasts 30-60 days, may not be sufficient time for FTB to determine whether the taxpayer is “innocent.” Amendment 4 would require FTB to release the proceeds if the taxpayer substantiates that they are an innocent investor and if the basis for that levy is the underpayment of any tax attributable to an abusive tax shelter.

4. The definition of “innocent partner” hinges on two elements: a partner who (1) did not engage in fraudulent acts, and (2) was not aware of any fraudulent acts. A determination of a partner’s innocence would be highly subjective. The taxpayer claiming innocent partner status would have to show that they were not aware of and did not engage in any fraudulent action that resulted in the underpayment of tax. It may be difficult to prove a negative proposition of this nature. In the *Hoyt* criminal case, the investors were not a part of the federal criminal litigation so there would be no legal findings of their “innocence.” Amendment 4 would define an innocent investor as one who had no responsibility for the creation, promotion, operation, management, or control of the abusive tax shelter and who was merely an investor. In addition, to qualify as “innocent,” the taxpayer would have not known that the entity, plan, or arrangement would be an abusive tax shelter.

5. The bill lists a “joint venture” as an entity in which a partner may be protected under this bill. A joint venture is only one of several entities that can be a partnership. Other entities that can be partnerships are syndicates, groups, pools, or other unincorporated organizations. To avoid confusion, Amendment 4 would remove the specific reference to “joint ventures” from the bill.

6. For liens on a principal residence to be released under this bill, the release is conditional on taxpayers establishing that they are innocent partners. However, the bill does not make it conditional that taxpayers establish innocence before FTB is prohibited from levying the taxpayer's principal residence. Amendment 4 would make the levy prohibition provision conditional on establishment of the "innocence" of the taxpayer.

7. The bill prohibits the levy on principal residences if the basis of the levy is a fraudulent act of another partner. However, the basis for a levy primarily is unpaid tax. Therefore, Amendment 4 clarifies that the basis for the levy in subdivision (a) would be the underpayment of any tax attributable to an abusive tax shelter.

8. Subdivision (c) of proposed new Section 21015.6 defines "innocent partner" in terms of a lien related to an underpayment of tax that is addressed in subdivision (b). The definition does not specifically apply to the levy provision in subdivision (a). Amendment 4 clarifies that the definition of "innocent investor" applies for purposes of both subdivisions.

9. A state tax lien recorded in the county where the principal residence is located would affect any real property transactions relating to that principal residence. The state tax lien only indirectly affects the escrow account. Amounts are disbursed to the department from the escrow account to satisfy, and for the title company to receive a release of, the state tax lien. Technically, a recorded state tax lien does not actually attach to nor would be released on escrow proceeds. Therefore, Amendment 4 would amend the bill to delete the reference under the lien provision to the escrow accounts and proceeds thereof, and would expressly require the FTB to release the lien on the principal residence without satisfaction of any portion of the property subject to the lien. However, in those rare instances where a notice of state tax lien has not been recorded by the time of a voluntary sale of real property, FTB could levy on the proceeds in escrow. Amendment 4 has provisions to require the release of such a levy and to require the return of any proceeds obtained through the levy.

10. This bill would prohibit a state tax lien recorded with a county recorder from attaching to property that qualifies as a declared homestead, unless the department has assessed a fraud penalty on the owners of the property. FTB does not generally assess fraud penalties. In addition, as amended, the bill would allow a recorded homestead declaration to defeat a recorded state tax lien for all taxpayers, not just a homeowner that is an innocent partner. Therefore, this bill would virtually allow all taxpayers to exempt their residence from a state tax lien. According to the author's staff, the intent of this bill is to allow only an "innocent partner" a release of lien on the principal residence, including those with declared homesteads. Amendments 1 and 3 would delete the language pertaining to the fraud penalty and the declared homestead.

LEGISLATIVE HISTORY

AB 2788 (Harris; Stats. 1988, Ch. 1573) established the TBR that is administered by the FTB.

SB 94 (Chesbro; Stats. 1999, Ch. 931) added additional TBR provisions that are generally the same as those enacted under federal law.

SB 685 (Monteith; Stats. 1999, Ch. 348) added additional TBR provisions relating to lien protections for the taxpayer. One provision is generally the same as that enacted under federal law; the other is an additional notice of tax lien requirement for certain situations.

PROGRAM BACKGROUND

According to the author's office, this bill is intended to help investors in partnerships like those described in the *Hoyt* criminal case that was recently reported in the newspapers. As reported, Hoyt was convicted on 52 counts relating to criminal activities in connection with what federal prosecutors indicated was one of the largest tax-shelter frauds in U.S. history. According to the news reports in *The Sacramento Bee*, June 8, 1999, and *The Oregonian*, February 18, 2001, some investors may have been financially devastated as a result of investments they made in Hoyt's various partnerships.

The *Hoyt* criminal case stemmed from IRS investigations and audits. Hoyt partnerships were in existence for approximately 20 years under varied degrees of activity. Because of the vast number of partnership entities (reportedly 94) and the complexities and magnitude of the transactions and intermingling of businesses, the IRS investigations and audits lasted many years.

The IRS sent the taxpayer-investors a settlement letter that proposes expediting the closing of the cases by both sides making certain concessions. In essence, the IRS agreed to not impose certain substantial penalties, to allow the partners a deduction for cash actually invested, and to disregard certain partnership income that may have been reported. The taxpayer had to concede Hoyt-related expenses, deductions, and credits, report certain Hoyt-partnership income, and accept certain higher interest rates.

FTB issued approximately 400 NPAs based on the Hoyt-RARs for 100 California residents. The average FTB Hoyt-based NPA is approximately $3,000 and does not include any penalties. However, the interest that has accrued over the number of years on these assessments may be significant. FTB is holding the finalization of the NPA and collection thereof pending the federal settlement and final determination. Several taxpayers, however, have asked that the California Hoyt-based NPAs be considered final and have resolved their case through an OIC.

OTHER STATES' INFORMATION

It does not appear that any state offers collection relief to investors in abusive tax shelters.

FISCAL IMPACT

The impact on departmental costs cannot be determined until the department has an opportunity to develop an implementation plan as it is unknown how much this bill would increase the workload of the department.

ECONOMIC IMPACT

Revenue Estimate

Based on available data and assumptions discussed below, this bill would result in a potential tax revenue loss of $6-$8 million annually after several years. As the bill would apply to liens that expire on and after January 1, 2002, the revenue loss would increase each year due to the increased number of each additional year's expired tax liens.

Estimated Revenue Impact of SB 366 As Amended 5/1/01 [$ In Millions]					
Provision	2001-02	2002-03	2003-04	2004-05	2005-06
Expiring liens	negligible loss	-$1	-$3	-$5	-$7
Innocent partners	negligible loss	-$0.5	-$0.5	-$0.5	-$0.5

Negligible loss is less than $250,000.

As the author's intent is to delete all provisions regarding "declared homestead," the estimate does not reflect any revenue effects with respect to these provisions.

Revenue Discussion

The revenue impact of this bill would be determined by the amount of foregone collections that would otherwise have resulted from (1) the department extending state tax liens beyond the initial 10-year period and (2) state tax liens recorded on either an innocent partner's principal residence or escrow or other accounts holding proceeds from the sale of an innocent partner's principal residence.

Expiring Liens

Each year, the department records 150,000 to 200,000 liens to secure tax debts. Of this total, collection staff estimates that about 10% of these accounts remain unsatisfied at the end of the initial 10-year period. Staff further estimates that about 20% of unsatisfied liens nearing expiration are extended an additional 10-years under current practice to continue to secure the tax debt. It is estimated that roughly 10% of account balances secured by liens extended an additional 10-years would eventually be collected. Most tax liens that would be extended to secure a tax debt an additional 10-years would have a higher than average account balance, perhaps ranging from a few thousand dollars to in excess of a million dollars. Assuming an average collection of $20,000 per account, foregone collections would be on the order of $6-$8 million annually after a number of years.

Innocent Partners

Circumstances placing a taxpayer in the position of an innocent partner, as defined, would appear to be rather limited. However, the bill would eliminate a collection tool in these limited circumstances.

When no other means of collection exists, a lien attaching to a principal residence secures the unresolved tax debt. In addition, a tax lien recorded before a bankruptcy petition is filed would survive a bankruptcy proceeding. Under these circumstances, a lien becomes the only means of securing a tax debt.

The department is currently holding (pending final federal determination) approximately 400 assessments issued to about 100 investors in partnerships who were California residents. Assessed taxes average approximately $3,000 per tax year and four tax years per investor (total of $12,000). Tax years at issue range from 1975 through 1994 with accrued interest increasing amounts due substantially. Each of these investors would fall into the innocent partner category of this bill.

However, if, in any given year, the total number of innocent partner liens for all relevant cases for which bankruptcy proceedings have been completed were 25, the amount of tax and interest potentially at risk would be around one-half million dollars (assuming an average balance due of $25,000).

As discussed under “Policy Considerations,” an amendment is being suggested to change the term “innocent partner” to “innocent investor.” Substituting the term investor would extend the provisions of this bill to individuals who are shareholders in other entities such as S corporations that invest in abusive tax shelters. An innocent investor also could include beneficiaries or trustees that have participated in fraudulent tax evasion schemes that are packaged as legitimate trusts, although it is unlikely many of these investors would meet the “did not know” criteria suggested in the amendment. The IRS estimates the federal government is losing billions of dollars of tax revenue from these fraudulent tax evasion schemes that are packaged as legitimate trusts. The IRS further indicates that a large percentage of these elaborate tax schemes to conceal income and create false business expenses for investors have gravitated to Northern California. To the extent these investors would fall into the innocent investor category of this bill, foregone collections of tax revenue would increase significantly.

ARGUMENTS/POLICY CONCERNS

Current laws and FTB practices, on a case-by-case basis, would provide tax relief to “Hoyt”-like taxpayers experiencing financial hardship and free their personal residence from levy and liens. Some may argue that current law and practice are sufficient to protect any of these "Hoyt" taxpayers who are truly “innocent partners.”

Many taxpayers that are not investors in abusive tax shelter partnerships experience devastating financial hardships. The intent of this bill is to offer tax collection protections to these certain partners beyond those given to other similarly situated taxpayers.

This bill would allow proceeds from a sale of the principal residence, regardless of the amount of the proceeds, to escape a recorded state tax lien. This policy would be in conflict with the law that allows liens to be released only if the release will not endanger or jeopardize the collection of taxes.

Currently, a homestead declaration protects only a certain amount of the proceeds from a voluntary sale from creditors. This bill protects the entire property from FTB but only for certain taxpayers. This conflicts with the concept of the homestead declaration under the Code of Civil Procedures.

This bill applies only to partners. There are individuals who invest in other types of entities such as S corporations that may be abusive tax shelters. These individuals would not receive the same tax collection protections. If the term "investors" were substituted for the term "partners" as discussed under “Implementation Considerations” and as shown in Amendment 4, this issue would be resolved.

There have been several recent efforts at the federal level to discourage corporations from investing in abusive tax shelters. These efforts have included regulatory action by the Treasury Department and the introduction of proposed federal legislation. While such legislation has not been enacted, this bill would move in the opposite direction by creating the possibility that taxpayers who invest in some of the most aggressive shelters may ultimately avoid paying the correct amount of tax.

This bill would prohibit only an income tax lien administered by FTB from being extended beyond 10 years. Other taxing agencies that file liens, such as the Board of Equalization and the Employment Development Department, would not be prohibited from extending their liens. The inability of the FTB to extend its liens subjects the department to loss of lien priority in relation to the other taxing agencies and judgment creditors.

This bill would not give any exceptions for extending the lien beyond 10 years, such as in the event of a NPA from an RAR and related protests and appeals, and bankruptcy cases. For instance, a substantial portion of the ten-year period may expire before the final federal audit determination is received by FTB or the bankruptcy matter is dismissed or discharged. The prohibition of the lien extension, without exception, would limit the flexibility of FTB in administering the state tax law and significantly affect tax collection.

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FRANCHISE TAX BOARD'S
PROPOSED AMENDMENTS TO SB 366
As Amended May 1, 2001

AMENDMENT 1

On page 2, strikeout lines 16 through 25, inclusive.

AMENDMENT 2

On page 3, line 37, strikeout "may" and insert:

shall

AMENDMENT 3

On page 4, strikeout lines 1 through 6, inclusive.

AMENDMENT 4

On page 4, modify lines 9 through 26, inclusive, as follows:

21015.6. (a)(1) No levy may be made on the principal residence of any innocent ~~partner~~investor or the proceeds from the sale or other transaction involving the principal residence of an innocent investor ~~if~~ upon substantiation of both of the following:
(A) ~~the~~The basis for that levy is an~~the fraudulent action of another partner~~underpayment of any tax imposed under Part 10 that is attributable to an abusive tax shelter.
(B) The principal residence is owned by an innocent investor.
(2) If, prior to the transmission of amounts in compliance with a levy on the proceeds from the sale or other transaction involving a principal residence described in paragraph (1), the owner of the principal residence has notified the Franchise Tax Board that the principal residence is owned by an innocent investor, amounts received pursuant to that levy shall be returned to the owner of the principal residence upon substantiation specified in paragraph (1).
(b)(1) Any state tax lien recorded ~~, as described~~ under Chapter 14 (commencing with Section 7150)~~, or Chapter 14.5 (commencing with Section 7220)~~ of Division 7 of Title 1 of the Government Code, including a state tax lien described under Title 11, Section 522(c)(2)(B) of the United States Code, relating to state tax liens after bankruptcy, on the principal residence of an innocent ~~partner~~investor~~or on an escrow or other account in which the proceeds from the sale of an innocent partner's principal residence are held~~, shall be released without satisfaction of the lien upon substantiation of both of the following:

(A) The ~~that~~underpayment of tax of an innocent investor is the basis for the lien.
(B) ~~the~~The owner of that principal residence is an innocent ~~partner~~investor.
(2) If, prior to satisfaction of a state tax lien described in paragraph (1), the owner of the principal residence subject to that lien has notified the Franchise Tax Board that the principal residence is owned by an innocent investor, amounts received pursuant to that state tax lien shall be returned to the owner of the principal residence upon substantiation specified in paragraph (1).

(c) For purposes of this section~~,~~:
(1) “Abusive tax shelter” must satisfy both of the following requirements:
(A) Be a potentially abusive tax shelter within the meaning of Section 6112 of the Internal Revenue Code.
(B) With respect to which either of the following has occurred:
(i) The Internal Revenue Service has imposed a penalty under Section 6700 or 6701 of the Internal Revenue Code, or
(ii) The Franchise Tax Board has imposed a penalty under Section 19177 or 19178.
(2) ~~an~~ “~~i~~Innocent ~~partner~~investor” means any individual (or the spouse or former spouse of that individual) that satisfies each of the following requirements: ~~partner or a spouse or former spouse of any partner~~
(A) Acquired an interest in ~~a partnership, limited partnership, or joint venture who did not engage in any fraudulent action~~ an abusive tax shelter prior to the date the Internal Revenue Service or the Franchise Tax Board imposed a penalty described in subparagraph (B) of paragraph (1).
(B) Is liable for ~~that resulted in the~~an underpayment of any tax imposed under Part 10 which is attributable to ownership of an interest in an abusive tax shelter.
(C) ~~to which the lien~~Had no responsibility for the creation, promotion, operation, management, or control of the abusive tax shelter.
(D) During the tax years to which the underpayment described in subparagraph (B) relates, did not know that the entity, plan, or arrangement would be an abusive tax shelter ~~was not aware of any fraudulent action, that resulted in the underpayment of any tax to which the lien relates~~.
(3) “Principal residence” includes any property that qualifies as a declared homestead as defined in Section 704.910 of the Code of Civil Procedures.

(d) Notification required by subdivisions (a) and (b) of this section shall be made at the time and in the manner prescribed in forms and instructions of the Franchise Tax Board.