

# ANALYSIS OF AMENDED BILL

Author: Fuller & Runner Analyst: Davi Milam Bill Number: SB 526  
 See Legislative  
 Related Bills: History Telephone: 845-2551 Amended Date: January 4, 2016  
 Attorney: Bruce Langston Sponsor \_\_\_\_\_

<b>SUBJECT:</b>	Innocent Spouse Relief/ Joint Returns/ Dissolution of Marriage Court Orders
-----------------	---

**SUMMARY**

Under the Administration Franchise and Income Tax Law (AFITL), this bill would modify provisions related to relief of joint liability by court order.

**RECOMMENDATION**

No position.

**Summary of Amendments**

The January 4, 2016, amendments removed provisions related to innocent spouse equitable relief and added the provisions discussed in this analysis.

This analysis replaces the department’s prior analysis of the bill as amended May 18, 2015.

**Summary of Suggested Amendments**

Technical amendments are suggested to change the indexing date.

**REASON FOR THE BILL**

The reason for this bill is to ease the financial burden of a spouse obtaining relief by divorce agreement and improve government efficiency by allowing the Franchise Tax Board (FTB) to honor a divorce order.

**EFFECTIVE/OPERATIVE DATE**

This bill would be effective January 1, 2017, and specifically operative for court orders served or acknowledged on or after that date.

**FEDERAL/STATE LAW**

Existing federal and state laws provide that taxpayers who file a joint return are each responsible for the accuracy of the tax return and are jointly and severally liable for the full tax liability due for

Board Position:	Executive Officer	Date									
<table style="width: 100%; border: none;"> <tr> <td style="width: 33%; border: none;"><u>      </u> S</td> <td style="width: 33%; border: none;"><u>      </u> NA</td> <td style="width: 33%; border: none;"><u>      </u> X</td> </tr> <tr> <td style="border: none;"><u>      </u> SA</td> <td style="border: none;"><u>      </u> O</td> <td style="border: none;"><u>      </u> NP</td> </tr> <tr> <td style="border: none;"><u>      </u> N</td> <td style="border: none;"><u>      </u> OUA</td> <td style="border: none;"><u>      </u> NAR</td> </tr> </table>	<u>      </u> S	<u>      </u> NA	<u>      </u> X	<u>      </u> SA	<u>      </u> O	<u>      </u> NP	<u>      </u> N	<u>      </u> OUA	<u>      </u> NAR	Selvi Stanislaus	01/13/16
<u>      </u> S	<u>      </u> NA	<u>      </u> X									
<u>      </u> SA	<u>      </u> O	<u>      </u> NP									
<u>      </u> N	<u>      </u> OUA	<u>      </u> NAR									

that tax year.<sup>1</sup> These obligations apply regardless of which spouse earns the income, or whether the correct amount of the tax is reported on the original return or whether the taxing authority subsequently assesses additional tax for the tax year in question. The concept of obligating each spouse individually for all of the tax liability is called joint and several liability. However, joint and several liability can result in inequitable consequences to one spouse in certain circumstances.

Consequently, both the federal government and California enacted “innocent spouse” legislation that may allow a spouse to be relieved of some or all of the responsibility for a joint tax debt.<sup>2</sup> Generally, the requesting spouse may not be relieved of tax liability on income that the requesting spouse earned or controlled. However, the Internal Revenue Service (IRS) may provide an exception to this general rule in situations where the nonrequesting spouse abused or exercised financial control over the requesting spouse.

State law, in addition to the “innocent spouse” provisions discussed above, also provides for relief when the liability has been revised by court order in a proceeding for dissolution of marriage.<sup>3</sup> The FTB will grant relief to the requesting spouse provided the order does not relieve the requesting spouse of tax liability on income earned by or subject to the exclusive management and control of that spouse.<sup>4</sup> The order is effective when the FTB is served with or acknowledges receipt of the order, and if the order:<sup>5</sup>

- Separately states the income tax liabilities for the taxable years for which revision of tax liability is granted.
- Does not revise a tax liability that has been fully paid prior to the effective date of the order.

Additionally, the requesting spouse must obtain from the FTB and file with the divorce court a tax revision clearance certificate (TRCC) if:

- Gross income reportable on the return exceeds one hundred and fifty thousand dollars (\$150,000), or
- The amount of tax liability the spouse is relieved of exceeds seven thousand five hundred dollars (\$7,500).

---

<sup>1</sup> Per Treasury Regulation 1.6013-4(b) this means that each spouse is liable for the entire joint tax liability; at the state level that provision is in Revenue and Taxation Code (R&TC) section 19006(b). Under state law, this provision also applies to registered domestic partners who file a joint tax return.

<sup>2</sup> Internal Revenue Code section 6015 and R&TC section 18533.

State law, under R&TC section 18533(i), also provides for relief based on IRS determination if applicable facts and circumstances are the same for federal and state income tax liabilities.

<sup>3</sup> R&TC section 19006(b).

<sup>4</sup> R&TC section 19006(b) (1).

<sup>5</sup> R&TC section 19006(b) (2).

## **THIS BILL**

This bill, under the AFITL, would provide that a court in, a proceeding for dissolution of marriage may not reduce the amount of liability on a joint return, but may revise the individual responsible for all or part of that liability.

This bill also would allow a court order issued in a proceeding for dissolution of marriage to relieve a spouse of liability on income earned by or subject to the exclusive management and control of that spouse, unless:

- Assets or liabilities are transferred between the individuals filing a joint return for the principal purpose of avoidance of the payment of tax or as part of a fraudulent scheme by those individuals.
- The liability is uncollectable, and within three years of when the FTB is served with or acknowledges receipt of the order, the spouse obligated by the court order does either of the following:
  - Files for bankruptcy and that liability is discharged in bankruptcy, or
  - Becomes a nonresident.

This bill also would increase the threshold amounts for a TRCC from gross income of \$150,000 to gross income of \$200,000 and for the amount of tax liability relieved from \$7,500 to \$10,000. Beginning in January 2017, the increased threshold amounts would be adjusted for inflation.

## **IMPLEMENTATION CONSIDERATIONS**

Implementing this bill would require some changes to existing tax forms and instructions and information systems, which could be accomplished during the normal annual update.

## **TECHNICAL CONSIDERATIONS**

Amendments 1 and 2 are provided to change the date indexing of the gross income and tax threshold amounts would begin.

## **LEGISLATIVE HISTORY**

SB 1065 (Walters, Chapter 318, Statutes of 2010) required the FTB to grant innocent spouse relief when the IRS has granted relief under the same facts and circumstances.

AB 1748 (Assembly Revenue and Taxation Committee, Chapter 342, Statutes of 2007) made changes to more closely conform California law to federal “innocent spouse” provisions and to provide the FTB the authority to issue guidelines and rules.

SB 285 (Speier, Chapter 370, Statutes of 2003) required the FTB to grant innocent spouse relief to an individual who had received an IRS grant of innocent spouse relief when the underlying facts and circumstances were the same. SB 285 was repealed by its own provisions effective January 1, 2009.

AB 2979 (Assembly Revenue and Taxation Committee, Chapter 374, Statutes of 2002) increased the gross income and tax liability thresholds for a TRCC to reflect inflation from 1977 to 2001, so that the amounts became \$150,000 for the gross income threshold and \$7,500 for the state income tax liability threshold.

## **OTHER STATES' INFORMATION**

The states surveyed include *Florida, Illinois, Massachusetts, Michigan, Minnesota, and New York*. These states were selected due to their similarities to California's economy, business entity types, and tax laws.

*Illinois, Massachusetts, Michigan, Minnesota, and New York* all provide innocent spouse relief; however, it is unclear whether the states provide relief comparable to the relief this bill would provide.

*Florida* does not have a personal income tax.

## **FISCAL IMPACT**

This bill would not significantly impact the department's costs.

## **ECONOMIC IMPACT**

### **Revenue Estimate**

This bill would result in a revenue impact to the general fund in an unknown amount.

### **Revenue Discussion**

According to calculations, for every \$1 million in tax liability relief granted, the revenue loss would be \$60,000. This bill does not reduce the amount of liability on a joint return, but instead allows a divorce court order to modify the amount of joint liability each spouse is responsible to pay.

Estimating cases of relief per divorce court order as part of the judgment for dissolution of marriage cannot be predicted. To determine the magnitude of relief, both the frequency and the dollar amount of these judgments must be known. Because it is difficult to predict the frequency and the value of future actions, the revenue impact is unknown.

## **SUPPORT/OPPOSITION<sup>6</sup>**

Support: George Runner, State Board of Equalization, Member.

The Executive Committee of the Family Law Section, the State Bar of California.

Opposition: None provided.

## **ARGUMENTS**

Proponents: Some may say this bill would assist taxpayers by providing greater assurance that the FTB will follow court orders granting relief.

Opponents: Some may argue that this bill is too broad and would be inconsistent with longstanding tax policy.

## **POLICY CONCERNS**

Taxpayers who file a joint return are jointly and severally liable for the full tax liability for the tax year(s) in which they filed jointly. Under state law, that liability may be revised by a divorce court, provided the order does not relieve the requesting spouse of tax liability on "income earned by or subject to the exclusive management and control of the requesting spouse." This condition reflects the longstanding tax policy of "proportional liability" (requesting spouse's pro rata share of tax liability on the requesting spouse's income). Applying a divorce order in all situations without regard to the concept of proportional liability would be contrary to this longstanding policy.

## **LEGISLATIVE STAFF CONTACT**

Davi Milam  
Legislative Analyst, FTB  
(916) 845-2551  
[davi.milam@ftb.ca.gov](mailto:davi.milam@ftb.ca.gov)

Jame Eiserman  
Revenue Manager, FTB  
(916) 845-7484  
[jame.eiserman@ftb.ca.gov](mailto:jame.eiserman@ftb.ca.gov)

Gail Hall  
Legislative Director, FTB  
(916) 845-6333  
[gail.hall@ftb.ca.gov](mailto:gail.hall@ftb.ca.gov)

---

<sup>6</sup> As noted in the Assembly Revenue and Taxation committee analysis dated July 10, 2015.

Analyst	Davi Milam
Telephone #	(916) 845-2551
Attorney	Bruce Langston

FRANCHISE TAX BOARD'S  
PROPOSED AMENDMENTS TO SB 526  
AS AMENDED JANUARY 4, 2016

AMENDMENT 1

On page 4, line 7, strikeout "2017" and insert:

2018

AMENDMENT 2

On page 4, line 10, strikeout "2017" and insert:

2018