

STATE OF ALABAMA  
DEPARTMENT OF REVENUE,

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STATE OF ALABAMA  
DEPARTMENT OF REVENUE  
ADMINISTRATIVE LAW DIVISION

§

v.

§

DOCKET NO. INC. 91-165

WILLIAM F. & RETHA JOHNSON  
P.O. Box 26  
Dozer, AL 36028,

§

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Taxpayers.

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FINAL ORDER

The Revenue Department assessed income tax against William and Retha Johnson (Taxpayers) for the years 1984 and 1985. Retha Johnson (Taxpayer) appealed to the Administrative Law Division and a hearing was conducted on May 27, 1992. The Taxpayer's attorney was notified of the hearing by certified mail on April 4, 1992, but failed to appear. Assistant counsel Mark Griffin represented the Department.

FINDINGS OF FACT

The Taxpayers filed joint Alabama income tax returns for the years 1984 and 1985 and reported total income of \$15,862.00 and \$20,138.00, respectively.

The IRS audited the Taxpayers' federal income tax returns for the subject years and determined that the Taxpayer William Johnson had received illegal gambling income of \$502,923.00 in 1984 and \$1,185,967.00 in 1985. The IRS audit was based on the Taxpayers' records and other relevant information.

The IRS report also indicated that the Taxpayer knew of her husband's gambling activities and was involved to the extent that

she co-signed loans for some of his customers. The Taxpayer had knowledge of the large cash flow through their joint checking account and was aware that she and her husband were spending much more than their reported income during the subject years. The Taxpayers' bank deposit records showed deposits of \$112,022.00 in 1984 and \$117,963.00 in 1985.

In addition to ordinary living expenses, the Taxpayers' also made extraordinary expenses during the subject years, including extensive remodeling of their house, numerous vacations to Florida and trips to Las Vegas, and the purchase of a car for cash in October 1984.

The Taxpayer concedes that her husband had unreported gambling income during the subject years but argues that she should not be liable for tax on the income because as an innocent spouse she had no personal knowledge and didn't benefit from the income.

#### CONCLUSIONS OF LAW

The "innocent spouse" rule is codified for federal purposes at 26 U.S.C.A. §6013 and for Alabama purposes at Code of Ala. 1975, §40-18-27. The rule provides that a spouse without knowledge of unreported income earned by the other spouse can under certain circumstances be relieved of liability on a joint return. The elements of the rule are (1) a joint return must be filed; (2) there must be a substantial understatement of income attributable to one spouse; (3) the other spouse must prove that he or she did

not know or have reason to know of the understatement; and (4) considering all of the facts, it would be inequitable to hold the other spouse liable for the tax attributable to the undisclosed income. The burden is on the one claiming innocent spouse status to prove each element of the rule. Shea v. C.I.R., 780 F.2d 561 (1986). The Taxpayer has not done so in this case.

The IRS report establishes a prima facie case that the Taxpayer knew or should have known of her husband's gambling income.<sup>1</sup> The Taxpayer has presented no evidence to the contrary.

Further, given the Taxpayer's involvement with her husband's activities and the fact that she benefited from the unreported income, it would be inequitable for the Taxpayer not to be liable on the assessment.

The above considered, the assessment in issue should be made final against both parties.

Entered on June 2, 1992.

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BILL THOMPSON  
Chief Administrative Law Judge

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<sup>1</sup>Whether the spouse benefited from the income was deleted as a specific element when §6013 was amended in 1984. However, that factor is important in deciding whether the spouse should in equity be relieved of liability.

