

MARK J. & CHARITY L. CHASTAIN  
27 DEAD TIMBERS ROAD  
DADEVILLE, AL 36853,

Taxpayers,

v.

STATE OF ALABAMA  
DEPARTMENT OF REVENUE.

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STATE OF ALABAMA  
DEPARTMENT OF REVENUE  
ADMINISTRATIVE LAW DIVISION

DOCKET NO. INC. 06-350

### **FINAL ORDER**

The Revenue Department assessed Mark J. and Charity L. Chastain (together “Taxpayers”) for 2003 income tax. Mark Chastain (individually “Taxpayer”) appealed to the Administrative Law Division pursuant to Code of Ala. 1975, §40-2A-7(b)(5)a. A hearing was conducted on August 9, 2006. The Taxpayer and Lynn Babbs attended the hearing. Assistant Counsel John Breckenridge represented the Department.

The issue in this case is whether the Taxpayer qualified for innocent spouse status concerning the 2003 liability pursuant to Code of Ala. 1975, §40-18-27(e). That statute provides that an innocent spouse shall be relieved of liability for Alabama income tax to the same extent allowed for federal purposes.

The Taxpayer and Charity Chastain were married and lived in Dadeville, Alabama during 2003. Charity worked for various local businesses as a cleaning woman. The Taxpayer worked for a pest exterminating business.

The couple had a joint checking account. The Taxpayer testified, however, that he knows nothing concerning finances, and that Charity maintained the checkbook and paid all of the bills. The Taxpayer knew his wife worked for various businesses as a cleaning woman, but had no idea how much she earned or what she did with her money.

The couple separated in September 2003. The Taxpayer thereafter learned that Charity had regularly used illegal drugs during their marriage. Charity went into a drug rehabilitation program soon after the separation. In the Fall of 2003, she began living with another man that had also been in drug rehab. Charity and the Taxpayer divorced in May 2004.

Charity prepared the couple's joint 2003 Alabama return before they divorced. She reported all of the Taxpayer's income, but failed to report all of her income on the return. The Taxpayer testified that Charity demanded that he sign the return. He did so without reviewing it because he was very intimidated by Charity, and also scared of the man she was living with.

Charity broke into the Taxpayer's trailer in mid-2004 and stole money and other items from him. She also withdrew all of the money from the Taxpayer's checking account. She was subsequently convicted of robbing a convenience store, and is now serving time in State prison. The Taxpayer has gotten by financially over the last two years only through the help of his employer.

The Department received information indicating that the Taxpayers had failed to report income on their joint 2003 return. It consequently assessed the Taxpayers jointly for the tax due. The Taxpayer claims he should be relieved of liability as an innocent spouse.

The Administrative Law Division addressed the innocent spouse relief provision in *Laney v. State of Alabama, Inc.* 02-156 (Admin. Law Div. 8/29/02):

As indicated, an Alabama taxpayer may be allowed innocent spouse status to the same extent allowed under federal law. Section 40-18-27(e). Under current federal law, a person qualifies as an innocent spouse (1) if they file a joint return which has an understatement of income due to erroneous items

of the spouse, (2) when they signed the joint return they did not know or have reason to know that there was an understatement of tax, and (3) taking into account all facts and circumstances, it would be unfair to hold the innocent spouse liable for tax on the unreported income. 26 U.S.C. §6015.<sup>1</sup> Whether the husband is entitled to innocent spouse status in this case turns on whether he knew or had reason to know that his wife had embezzled money during 1999. The “reason to know” standard was discussed in *Kistner v. Commissioner*, 18 F.3d 1521 (11th Cir. 1994), as follows:

A spouse has “reason to know” if a reasonably prudent taxpayer under the circumstances of the spouse at the time of signing the return could be expected to know that the tax liability stated was erroneous or that further investigation was warranted. *Stevens v. Commissioner of Internal Revenue* [89-1 USTC §9330], 872 F.2d 1499, 1505 (11th Cir. 1989). The test establishes a ‘duty of inquiry’ on the part of the alleged innocent spouse. *Stevens* [89-1 USTC §9330], 872 F.2d at 1505. The courts have recognized several factors that are relevant in determining the ‘reason to know,’ including (1) the alleged innocent spouse’s level of education; (2) the spouse’s involvement in the family’s business and financial affairs; (3) the presence of expenditures that appear lavish or unusual when compared to the family’s past levels of income, standard of income, and spending patterns; and (4) the culpable spouse’s evasiveness and deceit concerning the couple’s finances. *Stevens* [89-1 USTC §9330], 872 F.2d at 1505.

*Kistner*, 18 F.3d at 1525.

*Laney* at 3.

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<sup>1</sup>Before 1998, the federal innocent spouse provision was at 26 U.S.C. §6013(e). That section was repealed and the current innocent spouse provision at §6015(b) was enacted in 1998 as part of the IRS Restructuring and Reform Act of 1998 (P.L. 105-206). That legislation generally made it easier for individuals to qualify for innocent spouse relief. It also allows a spouse to elect for separation of liability treatment, §6015(c), and also equitable relief, §6015(f). However, Alabama law, at §40-18-27(e), only allows for innocent spouse relief. For a good explanation of the current federal statute, see, Harper, *Federal Tax Relief for Innocent Spouses: New Opportunities Under the IRS Restructuring and Reform Act of 1998*, 61 Ala.Law. 204 (May 2000).

The Taxpayer's ex-wife clearly omitted a portion of her income from the couple's joint 2003 return. The Taxpayer's innocent spouse status thus turns on (1) whether he knew when he signed the joint return that there was an understatement of income, and (2) would it be unfair or inequitable under the circumstances to hold the Taxpayer liable on the unreported income.

The Taxpayer is unsophisticated in financial matters and allowed his wife to handle their money during their marriage. His wife never told him how much she made or what she did with the money. Consequently, even if the Taxpayer had reviewed the couple's joint 2003 return before signing it, he would not have known that the amounts reported on the return were incorrect.

The Taxpayer is a mild mannered individual. It is thus understandable that he could have been intimidated by Charity and her boyfriend, both practicing drug addicts, into signing the return without reviewing it. Charity also obviously kept things from the Taxpayer because he did not know she was a drug addict until after they separated. Under the circumstances, it is believable that the Taxpayer did not know that his estranged wife had failed to report all of her income on the return.

The Taxpayer deposited his paychecks into the couple's joint checking account during their marriage. It is not known what his wife did with her earnings. It is reasonable to assume, however, that she spent some or all of the money on drugs, and not on the couple's joint expenses. There is also no evidence that his wife lived extravagantly or purchased expensive items, which might have alerted the Taxpayer that his wife was making money he did not know about.

Innocent spouse relief is an equitable remedy that must be applied to the particular facts of each case. Under the facts in this case, it would be inequitable to hold the Taxpayer liable for tax on income that his ex-wife probably spent on drugs, or at the least did not spend to the benefit of the Taxpayer. He is thus entitled to innocent spouse relief. That finding is supported by the fact that the IRS granted the Taxpayer separation of liability status for 2003. While Alabama law has not yet been conformed to also grant separation of liability status, it is similar to innocent spouse status in that it is an equitable remedy. The IRS thus also recognized that it would be inequitable to hold the Taxpayer personally liable for tax on his ex-wife's unreported income.

The Taxpayer is relieved of liability and is deleted from the final assessment in issue. The final assessment remains valid against the Taxpayer's ex-wife, Charity Chastain.

This Final Order may be appealed to circuit court within 30 days pursuant to Code of Ala. 1975, §40-2A-9(g).

Entered September 21, 2006.

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BILL THOMPSON  
Chief Administrative Law Judge

bt:dr

cc: John J. Breckenridge, Esq.  
Mark J. Chastain  
Joni Coman