

a.m. and 4 p.m., Monday through Friday.

The agency has determined under 21 CFR 25.33(a)(2) that this action is of a type that does not individually or cumulatively have a significant effect on the human environment. Therefore, neither an environmental assessment nor an environmental impact statement is required.

This rule does not meet the definition of "rule" in 5 U.S.C. 804(3)(A) because it is a rule of "particular applicability." Therefore, it is not subject to the congressional review requirements in 5 U.S.C. 801-808.

#### List of Subjects in 21 CFR Part 558

Animal drugs, Animal feeds.

■ Therefore, under the Federal Food, Drug, and Cosmetic Act and under authority delegated to the Commissioner of Food and Drugs and redelegated to the Center for Veterinary Medicine, 21 CFR part 558 is amended as follows:

#### PART 558—NEW ANIMAL DRUGS FOR USE IN ANIMAL FEEDS

■ 1. The authority citation for 21 CFR part 558 continues to read as follows:

**Authority:** 21 U.S.C. 360b, 371.

■ 2. Section 558.550 is amended by adding paragraph (a)(3); and in paragraph (d)(1)(xv)(c) by removing "and 046573" and by adding in its place "and 053389" to read as follows:

#### § 558.550 Salinomycin.

(a) \* \* \*

(3) To 053389 for use as in paragraph (d)(1)(xv) of this section.

\* \* \* \* \*

Dated: June 26, 2003.

**Andrew J. Beaulieu,**

*Acting Director, Center for Veterinary Medicine.*

[FR Doc. 03-17409 Filed 7-9-03; 8:45 am]

**BILLING CODE 4160-01-S**

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## DEPARTMENT OF THE TREASURY

### Internal Revenue Service

#### 26 CFR Parts 1 and 602

[TD 9074]

RIN 1545-AY83

#### Treatment of Community Income for Certain Individuals Not Filing Joint Returns

**AGENCY:** Internal Revenue Service (IRS), Treasury.

**ACTION:** Final regulations.

**SUMMARY:** This document contains final regulations relating to the treatment of community income under Internal Revenue Code section 66 for certain married individuals in community property states who do not file joint Federal income tax returns. The final regulations also reflect changes in the law made by the Internal Revenue Service Restructuring and Reform Act of 1998.

**EFFECTIVE DATE:** These final regulations are effective July 10, 2003.

**FOR FURTHER INFORMATION CONTACT:** Robin M. Tuczak, 202-622-4940 (not a toll-free number).

#### SUPPLEMENTARY INFORMATION:

##### Paperwork Reduction Act

The collection of information contained in the final regulations has been reviewed and approved by the Office of Management and Budget in accordance with the Paperwork Reduction Act of 1995 (44 U.S.C. 3507) under control number 1545-1770. Responses to this collection of information are required in order for certain individuals to receive relief from the operation of community property law.

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection of information displays a valid control number assigned by the Office of Management and Budget.

Estimated total annual reporting burden for 2001 for Form 8857, "Request for Innocent Spouse Relief": 21,123 hours.

Estimated average annual burden hours per response: 59 minutes.

Estimated number of responses for 2001 for Form 8857: 21,336.

Requests for relief under section 66(c) constitute less than 1% of the total requests filed using Form 8857.

Comments on the collection of information should be sent to the Office of Management and Budget, Attn: Desk Officer for the Department of the Treasury, Office of Information and Regulatory Affairs, Washington, DC 20503, with copies to the Internal Revenue Service, Attn: IRS Reports Clearance Officer, W:CAR:MP:T:T:SP, Washington, DC 20224.

Books or records relating to a collection of information must be retained as long as their contents may become material in the administration of any internal revenue law. Generally, tax returns and return information are confidential, as required by section 6103 of the Internal Revenue Code (Code).

#### Background

This document contains amendments to 26 CFR part 1 under section 66 of the Code, relating to the treatment of community income for certain individuals not filing joint returns. For rules regarding relief from joint and several liability when a joint return is filed, see section 6015 and the regulations thereunder.

A notice of proposed rulemaking (REG-115054-01) was published in the **Federal Register** (67 FR 2841) on January 22, 2002. No public hearing was requested or held. Written comments responding to the notice of proposed rulemaking were received. After consideration of all the comments, the proposed regulations are adopted as amended by this Treasury Decision. The comments and revisions are discussed below.

#### Explanation and Summary of Comments

##### 1. General

One commentator suggested that the proposed regulations under section 66 (particularly § 1.66-2) were not helpful, given the community property laws of the commentator's state. This commentator also suggested that the proposed regulations appear to assume that the community property laws of all community property states are the same. The intent of these regulations is not to provide guidance based on the community property laws of any particular state. Instead, the regulations provide guidance on the effect of section 66 on taxpayers' community income as determined under state law. After a determination that an item of income is community income under state law, these regulations provide guidance on the treatment of this income under section 66 for certain individuals not filing joint returns.

One commentator noted that there are fundamental differences between married taxpayers who filed joint returns and request relief from joint and several liability under section 6015 and married taxpayers who filed separate returns and request relief from the Federal income tax liability resulting from the operation of community property law under section 66(c).

The final regulations do not address differences between or make generalizations concerning married taxpayers who file joint returns and those who do not. The final regulations focus on providing guidance on the treatment of community income for certain taxpayers under section 66.

The preamble to the proposed regulations under section 66 references

the spousal notification requirements set forth in regulations under section 6015 and discusses similar notification requirements under section 66. If the IRS grants relief under section 66, the liability of the requesting spouse will shift to the nonrequesting spouse. Thus, notification and participation requirements similar to those applicable in section 6015 cases are also appropriate for section 66 cases. In addition, information provided by a nonrequesting spouse may help to determine the appropriate amount of relief for the requesting spouse, if any.

Similarities between the guidance set forth in the regulations under section 6015 and the regulations under section 66 are due to the similarities in the elements required, or factors considered, in determining relief under these statutes. The analysis set forth in proposed § 1.66-4(a)(2) and (3) regarding knowledge or reason to know and benefit is similar to that contained in § 1.6015-2(c) and (d). The final regulations modify this analysis and adopt commentators' suggestions to the extent that the suggestions are consistent with the statute, legislative history, and case law under section 66(c). These changes are more fully discussed in the comments and explanation under § 1.66-4 below.

## 2. Section 1.66-1

One commentator stated that § 1.66-1 of the proposed regulations failed to expressly require each of the spouses to report those items of separate income that are attributable to each spouse under applicable state community property laws. Generally, community income is reportable half by each spouse pursuant to *Poe v. Seaborn*, 282 U.S. 101 (1930), and section 61. Whether income is separate or community is determined under state law and the income is included in gross income under section 61. The final regulations do not include guidance on how to report income that is not community income under state law, as this would be outside the scope of section 66.

The final regulations clarify in § 1.66-1(a) that the general rule of community property applies to married individuals domiciled in community property states. A taxpayer should report income in accordance with the laws of the state in which he or she is domiciled. *United States v. Mitchell*, 403 U.S. 190, 197 (1971); *Commissioner v. Wilkerson*, 368 F.2d 552, 553 (9th Cir. 1966). For example, a taxpayer who is domiciled in State A, a community property state, should report income in accordance with the community property laws of State A, although she may be living in

State B temporarily, due to a work detail, military assignment, etc.

One commentator noted that under § 1.66-1(b), the limitation of the scope of the regulations to married taxpayers was too restrictive. The commentator noted that income earned during a marriage, but received after the dissolution of the marital community, was community income under the laws of the commentator's state. The commentator suggested that section 66 should apply to this income, as it is community income under state law. The final regulations frame the issue in terms of application of section 66 to community income, rather than in terms of marital status.

The final regulations state that section 66 applies only to community income, as defined by state law. The final regulations, however, make a distinction between community income and income from property that was formerly community property but, in accordance with state law, is converted to a form of property that is not community property, such as separate property or property held by joint tenancy or tenancy in common.

Under the laws of certain community property states, property that was community property during the marriage ceases to be community property after the dissolution of the marital community. Conversely, some state laws treat property that was not community property as community property for the limited purpose of dividing assets upon divorce. See *Estate of Mitchell v. Mitchell*, 76 Cal. App. 4th 1378 (Cal. Ct. App. 1999). Income from such property is not community income subject to the provisions of section 66. The determination as to whether income from such property is community income may be confusing due to the fact that sometimes courts will refer to the property, using "universally recognized shorthand," as community property. See *Bouterie v. Commissioner*, 36 F.3d 1361 (5th Cir. 1994) (in which the court found that the wife did not have community income from community property and the IRS improperly relied on a state court's imprecise use of the term "community property" in referring to property that was formerly community property), *rev'g* T.C. Memo. 1993-510.

Thus, in determining whether section 66 applies to income, it is first necessary to determine whether the income is community income under state law. The marital status of the parties likely will be relevant to this initial determination.

## 3. Section 1.66-2

One commentator noted that it may be difficult to determine whether a transfer of income is a transfer of earned income under § 1.66-2(a)(5). A transfer of earned income precludes the reporting of income in accordance with § 1.66-2, even if a taxpayer meets the other requirements of § 1.66-2. The commentator suggested that there should be a presumption under § 1.66-2 that any transfer of income or property is a transfer of earned income. The final regulations adopt this recommendation with respect to transfers of income. It is a logical presumption that income is more likely to be earned than unearned, and that a taxpayer who has unearned income is likely to have earned income as well.

Another commentator suggested that the final regulations clarify the requirement of § 1.66-2 that spouses live apart. The final regulations adopt this recommendation by cross-referencing the definition of members of the same household in § 1.6015-3(b).

The final regulations clarify that, when reporting income in accordance with section 66(a), an individual must report all income in accordance with section 66(a). Section 66(a) does not apply on an item-by-item basis.

## 4. Section 1.66-3

One commentator recommended that the final regulations emphasize that the IRS may disallow the Federal income tax benefits of any community property law under section 66(b) on an item-by-item basis. Because the proposed regulations already reference "item of community income" in every sentence of § 1.66-3, however, the final regulations do not adopt this recommendation.

One commentator suggested that the IRS should assert section 66(b) sparingly, only if "the \* \* \* spouse had no knowledge whatever of the income \* \* \* and did not benefit from the income in a division of marital assets." Section 66(b) allows the IRS to deny the Federal income tax benefits of community property law only when a taxpayer acted as if solely entitled to the income and failed to notify the taxpayer's spouse of the income. The final regulations do not impose additional requirements on the IRS.

Commentators also recommended that the final regulations provide examples of what constitutes treating income as solely one's own and how specific a taxpayer must be when notifying his or her spouse of the nature and amount of the income. The final regulations adopt this recommendation.

##### 5. Section 1.66-4

The proposed regulations describe relief granted under the first sentence of section 66(c) as “specific relief.” The final regulations adopt the term *traditional relief* to describe relief granted under this provision. The final regulations retain the term “equitable relief” to describe the relief granted under the second sentence of section 66(c).

The proposed regulations require that a spouse requesting relief under § 1.66-4 file a separate return for the taxable year relating to the request. One commentator noted that section 66(c)(1) requires only that an individual not file a joint return. The legislative history of section 66(c) confirms that Congress did not intend to require an individual to file a return to be eligible for relief under this provision. The House Report uses the phrase “at the time the return was filed (if a return is filed).” H.R. Rep. No. 98-432, pt. 2, at 1503 (1984). In earlier cases regarding relief under section 66(c), the Tax Court implies that a requesting spouse must file a separate return. See, e.g., *Roberts v. Commissioner*, T.C. Memo. 1987-391, *aff'd* 860 F.2d 1235 (5th Cir. 1988). More recent cases, however, specifically state that not filing any return meets the requirement of not filing a joint return. See, e.g., *Ollestad v. Commissioner*, T.C. Memo. 1996-139; *Costa v. Commissioner*, T.C. Memo. 1990-572. The final regulations adopt the recommendation to limit the requirement to not filing a joint return.

One commentator suggested that the discussion of knowledge and reason to know of an item of community income in § 1.66-4 ignores the low probability that a requesting spouse would have access to accurate information or knowledge regarding what the nonrequesting spouse reported or did not report for Federal income tax purposes. Under section 66(c), a requesting spouse is required to prove, among other things, that “he or she did not know of, and had no reason to know of, such item of community income” to obtain traditional relief. The final regulations include a discussion of knowledge and reason to know, as this is an element required by section 66(c)(3). The facts and circumstances considered in making the determination of knowledge or reason to know are consistent with the knowledge and reason to know analysis set forth in case law determining relief under section 66(c).

Additionally, the final regulations include new language regarding the knowledge standard under section 66(c).

To more closely track the language of section 66(c), the phrase *item of community income* replaces the term *understatement* when referring to the item about which the requesting spouse has knowledge or reason to know. Finally, the final regulations clarify that knowledge of the source of community income or the income-producing activity, without knowledge of the specific amount of income, is sufficient knowledge to preclude relief under section 66(c). This is consistent with the knowledge and reason to know analysis set forth in case law under section 66(c). See, e.g., *McGee v. Commissioner*, 979 F.2d 66, 70 (5th Cir. 1992), *aff'g* T.C. Memo. 1991-510.

Two commentators questioned whether the standard of significant benefit in excess of normal support, which is used in determining whether it is equitable to grant relief under section 6015, is the applicable standard under section 66. One commentator noted that under community property laws, each spouse generally is entitled to half of the income of the other spouse. Under section 66, a requesting spouse essentially is seeking relief for half the income of both spouses, which may have been used to provide normal support to both spouses. Contrast this situation to that under section 6015, which permits a requesting spouse to seek relief from joint and several liability for the tax on all of the income of the nonrequesting spouse. This commentator suggested that the tax liability should be shifted to the nonrequesting spouse only if the nonrequesting spouse has treated the income in a manner inconsistent with the community property regime, for example, has not allowed use of the income for normal support or has transferred no part of the income to the requesting spouse.

A majority of cases decided under section 66(c) make the determination of whether it is equitable to grant relief based on the “benefit” received by the requesting spouse, as opposed to the “significant benefit” standard applied by courts in determining relief under former section 6013(e) and section 6015(b). See *Beck v. Commissioner*, T.C. Memo. 2001-198, *acq.* 2002-49 I.R.B.; *Hardy v. Commissioner*, T.C. Memo. 1997-97. The court in *Beck* and *Hardy* cited the legislative history of section 66(c) when discussing benefit under section 66. The legislative history provides that, in determining whether it is equitable to grant relief under section 66(c), the standard is “whether the [requesting] spouse benefitted from the untaxed income.” H. Rep. No. 98-432,

pt. 2, at 1503 (1984). The final regulations adopt this standard.

One commentator suggested that the time limitations set forth in § 1.66-4 for requesting relief under section 66(c) are not supported by the language of section 66(c). Although the statute itself does not set forth time limitations on the filing of a request for relief, the time limitations in the proposed regulations are supported by the legislative history of the traditional relief provision of section 66(c). Specifically, the House Report explaining traditional relief under section 66(c) states that, in making the determination as to relief, the IRS should consider (among other things) “whether the defense was promptly raised so as to prevent the period of limitations from running on the other spouse.” H.R. Rep. No. 98-432, pt. 2, at 1501 (1984). Thus, the final regulations retain the time limitations set forth in the proposed regulations. In contrast, § 1.66-4(j)(2)(ii) sets forth timing requirements for requesting equitable relief that are broader than the requirements applicable to traditional relief because the legislative history of the equitable relief provision does not contain similar timing requirements. Therefore, a requesting spouse who does not meet the time limitations to request traditional relief may be eligible to request equitable relief.

Another commentator noted that perhaps the timeliness of the requesting spouse’s request should be only one factor in determining whether to grant traditional relief under section 66(c), as opposed to a threshold requirement. This comment was not adopted because a requesting spouse who does not meet the timing requirements for traditional relief still may receive equitable relief under section 66(c).

One commentator urged that no request for relief under section 66 should be considered premature. There must be some indication that the IRS may determine a deficiency prior to the filing of a request for relief from a deficiency under section 66(c). Thus, the final regulations retain the timing limitations set forth in the proposed regulations regarding premature requests.

The final regulations incorporate an item-by-item approach to relief from the Federal income tax liability resulting from the operation of community property law under section 66(c). If a requesting spouse receives relief under section 66(c), the proposed regulations provide for treatment of *any* community income of the spouses in accordance with the rules provided by section 879(a), which is consistent with the statutory rule under section 66(a). The

final regulations provide that if a requesting spouse receives relief for an item, the rules provided by section 879(a) will govern the treatment of the item. The item-by-item approach adopted in the final regulations is consistent with the statutory language in section 66(c) that states "such item of community income shall be included in the gross income of the other spouse (and not in the gross income of the individual)." (Emphasis added.)

Traditionally, section 66(c) provided relief from liability resulting only from items of income, unlike former section 6013(e) and section 6015. The final regulations expand equitable relief under § 1.66-4(b) to include relief for underpayments of tax or any deficiency, including those arising from disallowed deductions or credits. This is consistent with the equitable relief provision in section 66(c).

### Special Analyses

It has been determined that these final regulations are not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It has also been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to the regulations, and because the regulations do not impose a collection of information on small entities, the Regulatory Flexibility Act (5 U.S.C. chapter 6) does not apply.

### Drafting Information

The principal author of the regulations is Robin M. Tuczak of the Office of Associate Chief Counsel (Procedure and Administration), Administrative Provisions and Judicial Practice Division.

### List of Subjects

#### 26 CFR Part 1

Income taxes, Reporting and recordkeeping requirements.

#### 26 CFR Part 602

Reporting and recordkeeping requirements.

### Adoption of Amendments to the Regulations

Accordingly, 26 CFR parts 1 and 602 are amended as follows:

## PART 1—INCOME TAXES

■ **Paragraph 1.** The authority citation for part 1 is amended by adding an entry in numerical order to the table to read in part as follows:

**Authority:** 26 U.S.C. 7805 \* \* \*

Section 1.66-4 also issued under 26 U.S.C. 66(c). \* \* \*

■ **Par. 2.** Sections 1.66-1 through 1.66-5 are added to read as follows:

### § 1.66-1 Treatment of community income.

(a) *In general.* Married individuals domiciled in a community property state who do not elect to file a joint individual Federal income tax return under section 6013 generally must report half of the total community income earned by the spouses during the taxable year except at times when one of the following exceptions applies:

(1) The spouses live apart and meet the qualifications of § 1.66-2.

(2) The Secretary denies a spouse the Federal income tax benefits resulting from community property law under § 1.66-3, because that spouse acted as if solely entitled to the income and failed to notify his or her spouse of the nature and amount of the income prior to the due date for the filing of his or her spouse's return.

(3) A requesting spouse qualifies for traditional relief from the Federal income tax liability resulting from the operation of community property law under § 1.66-4(a).

(4) A requesting spouse qualifies for equitable relief from the Federal income tax liability resulting from the operation of community property law under § 1.66-4(b).

(b) *Applicability.* (1) The rules of this section apply only to community income, as defined by state law. The rules of this section do not apply to income that is not community income. Thus, the rules of this section do not apply to income from property that was formerly community property, but in accordance with state law, has ceased to be community property, becoming, *e.g.*, separate property or property held by joint tenancy or tenancy in common.

(2) When taxpayers report income under paragraph (a) of this section, *all* community income for the calendar year is treated in accordance with the rules provided by section 879(a). Unlike the other provisions under section 66, section 66(a) does not permit inclusion on an item-by-item basis.

(c) *Transferee liability.* The provisions of section 66 do not negate liability that arises under the operation of other laws. Therefore, a spouse who is not subject to Federal income tax on community income may nevertheless remain liable for the unpaid tax (including additions to tax, penalties, and interest) to the extent provided by Federal or state transferee liability or property laws (other than community property laws). For the rules regarding the liability of

transferees, see sections 6901 through 6904 and the regulations thereunder.

### § 1.66-2 Treatment of community income where spouses live apart.

(a) Community income of spouses domiciled in a community property state will be treated in accordance with the rules provided by section 879(a) if all of the following requirements are satisfied—

(1) The spouses are married to each other at any time during the calendar year;

(2) The spouses live apart at all times during the calendar year;

(3) The spouses do not file a joint return with each other for a taxable year beginning or ending in the calendar year;

(4) One or both spouses have earned income that is community income for the calendar year; and

(5) No portion of such earned income is transferred (directly or indirectly) between such spouses before the close of the calendar year.

(b) *Living apart.* For purposes of this section, living apart requires that spouses maintain separate residences. Spouses who maintain separate residences due to temporary absences are not considered to be living apart. Spouses who are not members of the same household under § 1.6015-3(b) are considered to be living apart for purposes of this section.

(c) *Transferred income.* For purposes of this section, transferred income does not include a *de minimis* amount of earned income that is transferred between the spouses. In addition, any amount of earned income transferred for the benefit of the spouses' child will not be treated as an indirect transfer to one spouse. Additionally, income transferred between spouses is presumed to be a transfer of earned income. This presumption is rebuttable.

(d) *Examples.* The following examples illustrate the rules of this section:

*Example 1. Living apart.* H and W are married, domiciled in State A, a community property state, and have lived apart the entire year of 2002. W, who is in the Army, was stationed in Korea for the entire calendar year. During their separation, W intended to return home to H, and H intended to live with W upon W's return. H and W do not file a joint return for taxable year 2002. H and W may not report their income under this section because a temporary absence due to military service is not living apart as contemplated under this section.

*Example 2. Transfer of earned income—de minimis exception.* H and W are married, domiciled in State B, a community property state, and have lived apart the entire year of 2002. H and W are estranged and intend to live apart indefinitely. H and W do not file

a joint return for taxable year 2002. H occasionally visits W and their two children, who live with W. When H visits, he often buys gifts for the children, takes the children out to dinner, and occasionally buys groceries or gives W money to buy the children new clothes for school. Both W and H have earned income in the year 2002 that is community income under the laws of State B. H and W may report their income on separate returns under this section.

*Example 3. Transfer of earned income—source of transfer.* H and W are married, domiciled in State C, a community property state, and have lived apart the entire year of 2002. H and W are estranged and intend to live apart indefinitely. H and W do not file a joint return for taxable year 2002. W provides H \$1,000 a month from March 2002 through August 2002 while H is working part-time and seeking full-time employment. W is not legally obligated to make the \$1,000 payments. W earns \$75,000 in 2002 in wage income. W also receives \$10,000 in capital gains income in December 2002. H wants to report his income in accordance with this section, alleging that the \$6,000 that he received from W was not from W's earned income, but from the capital gains income W received in 2002. The facts and circumstances surrounding the periodic payments to H from W do not indicate that W made the payments out of her capital gains. H and W may not report their income in accordance with this section, as the \$6,000 W transferred to H is presumed to be from W's earned income, and H has not presented any facts to rebut the presumption.

**§ 1.66-3 Denial of the Federal income tax benefits resulting from the operation of community property law where spouse not notified.**

(a) *In general.* The Secretary may deny the Federal income tax benefits of community property law to any spouse with respect to any item of community income if that spouse acted as if solely entitled to the income and failed to notify his or her spouse of the nature and amount of the income before the due date (including extensions) for the filing of the return of his or her spouse for the taxable year in which the item of income was derived. Whether a spouse has acted as if solely entitled to the item of income is a facts and circumstances determination. This determination focuses on whether the spouse used, or made available, the item of income for the benefit of the marital community.

(b) *Effect.* The item of community income will be included, in its entirety, in the gross income of the spouse to whom the Secretary denied the Federal income tax benefits resulting from community property law. The tax liability arising from the inclusion of the item of community income must be assessed in accordance with section 6212 against this spouse.

(c) *Examples.* The following examples illustrate the rules of this section:

*Example 1. Acting as if solely entitled to income.* (i) H and W are married and are domiciled in State A, a community property state. W's Form W-2 for taxable year 2000 showed wage income of \$35,000. W also received a Form 1099-INT, "Interest Income," showing \$1,000 W received in taxable year 2000. W's wage income was directly deposited into H and W's joint account, from which H and W paid bills and household expenses. W did not inform H of her interest income or the Form 1099-INT, but W gave H a copy of the W-2 when she received it in January 2001. W did not use her interest income for bills or household expenses. Instead W gave her interest income to her brother, who was unemployed. Neither the separate return filed by H nor the separate return filed by W included the interest income. In 2002, the IRS audits both H and W. The Internal Revenue Service (IRS) may raise section 66(b) as to W's interest income, denying W the Federal income tax benefit resulting from community property law as to this item of income.

(ii) H and W are married and are domiciled in State B, a community property state. For taxable year 2000, H receives \$45,000 in wage income that H places in a separate account. H and W maintain separate residences. H's wage income is community income under the laws of State B. That same year, W loses her job, and H pays W's mortgage and household expenses for several months while W seeks employment. Neither H nor W files a return for 2000, the taxable year for which the IRS subsequently audits them. The IRS may not raise section 66(b) and deny H the Federal income tax benefits resulting from the operation of community property law as to H's wage income of \$45,000, as H has not treated this income as if H were solely entitled to it.

*Example 2. Notification of nature and amount of the income.* H and W are married and domiciled in State C, a community property state. H and W do not file a joint return for taxable year 2001. H's and W's earned income for 2001 is community income under the laws of State C. H receives \$50,000 in wage income in 2001. In January 2002, H receives a Form W-2 that erroneously states that H earned \$45,000 in taxable year 2001. H provides W a copy of H's Form W-2 in February 2002. W files for an extension prior to April 15, 2002. H receives a corrected Form W-2 reflecting wages of \$50,000 in May 2002. H provides a copy of the corrected Form W-2 to W in May 2002. W files a separate return in June 2002, but reports one half of \$45,000 (\$22,500) of wage income that H earned. H files a separate return reporting half of \$50,000 (\$25,000) in wage income. The IRS audits both H and W. Even if H had acted as if solely entitled to the wage income, the IRS may not raise section 66(b) as to this income because H notified W of the nature and amount of the income prior to the due date of W's return (including extensions).

**§ 1.66-4 Request for relief from the Federal income tax liability resulting from the operation of community property law.**

(a) *Traditional relief—(1) In general.* A requesting spouse will receive relief from the Federal income tax liability resulting from the operation of community property law for an item of community income if—

(i) The requesting spouse did not file a joint Federal income tax return for the taxable year for which he or she seeks relief;

(ii) The requesting spouse did not include in gross income for the taxable year an item of community income properly includible therein, which, under the rules contained in section 879(a), would be treated as the income of the nonrequesting spouse;

(iii) The requesting spouse establishes that he or she did not know of, and had no reason to know of, the item of community income; and

(iv) Taking into account all of the facts and circumstances, it is inequitable to include the item of community income in the requesting spouse's individual gross income.

(2) *Knowledge or reason to know.* (i) A requesting spouse had knowledge or reason to know of an item of community income if he or she either actually knew of the item of community income, or if a reasonable person in similar circumstances would have known of the item of community income. All of the facts and circumstances are considered in determining whether a requesting spouse had reason to know of an item of community income. The relevant facts and circumstances include, but are not limited to, the nature of the item of community income, the amount of the item of community income relative to other income items, the couple's financial situation, the requesting spouse's educational background and business experience, and whether the item of community income was reflected on prior years' returns (e.g., investment income omitted that was regularly reported on prior years' returns).

(ii) If the requesting spouse is aware of the source of community income or the income-producing activity, but is unaware of the specific amount of the nonrequesting spouse's community income, the requesting spouse is considered to have knowledge or reason to know of the item of community income. The requesting spouse's lack of knowledge of the specific amount of community income does not provide a basis for relief under this section.

(3) *Inequitable.* All of the facts and circumstances are considered in determining whether it is inequitable to

hold a requesting spouse liable for a deficiency attributable to an item of community income. One relevant factor for this purpose is whether the requesting spouse benefitted, directly or indirectly, from the omitted item of community income. A benefit includes normal support, but does not include *de minimis* amounts. Evidence of direct or indirect benefit may consist of transfers of property or rights to property, including transfers received several years after the filing of the return. Thus, for example, if a requesting spouse receives from the nonrequesting spouse property (including life insurance proceeds) that is traceable to items of community income attributable to the nonrequesting spouse, the requesting spouse will have benefitted from those items of community income. Other factors may include, if the situation warrants, desertion, divorce or separation. Factors relevant to whether it would be inequitable to hold a requesting spouse liable, more specifically described under the applicable administrative procedure issued under section 66(c) (Revenue Procedure 2000-15 (2000-1 C.B. 447) (See § 601.601(d)(2) of this chapter), or other applicable guidance published by the Secretary), are to be considered in making a determination under this paragraph.

(b) *Equitable relief.* Equitable relief may be available when the four requirements of paragraph (a)(1) of this section are not satisfied, but it would be inequitable to hold the requesting spouse liable for the unpaid tax or deficiency. Factors relevant to whether it would be inequitable to hold a requesting spouse liable, more specifically described under the applicable administrative procedure issued under section 66(c) (Revenue Procedure 2000-15 (2000-1 C.B. 447), or other applicable guidance published by the Secretary), are to be considered in making a determination under this paragraph.

(c) *Applicability.* Traditional relief under paragraph (a) of this section applies only to deficiencies arising out of items of omitted income. Equitable relief under paragraph (b) of this section applies to any deficiency or any unpaid tax (or any portion of either). Equitable relief is available only for the portion of liabilities that were unpaid as of July 22, 1998, and for liabilities that arise after July 22, 1998.

(d) *Effect of relief.* When the requesting spouse qualifies for relief under paragraph (a) or (b) of this section, the IRS must assess any deficiency of the nonrequesting spouse arising from the granting of relief to the

requesting spouse in accordance with section 6212.

(e) *Examples.* The following examples illustrate the rules of this section:

*Example 1. Item-by-item approach.* H and W are married, living together, and domiciled in State A (a community property state). H and W file separate returns for taxable year 2002 on April 15, 2003. H earns \$56,000 in wages, and W earns \$46,000 in wages, in 2002. H reports half of his wage income as shown on his Form W-2, in the amount of \$28,000, and half of W's wage income as shown on her Form W-2, in the amount of \$23,000. W reports half of her wage income as shown on her W-2, in the amount of \$23,000, and half of H's wage income as shown on his Form W-2, in the amount of \$28,000. Neither H nor W reports W's income from her sole proprietorship of \$34,000 or W's investment income of \$5,000 for taxable year 2002. The Internal Revenue Service (IRS) proposes deficiencies with respect to H's and W's taxable year 2002 returns due to the omission of W's income from her sole proprietorship and investments. H timely requests relief under section 66(c). Because the IRS determines that H satisfies the four requirements of the traditional relief provision of section 66(c) with respect to W's omitted investment income, the IRS grants H's request for relief as to the omitted investment income. The IRS determines that H does not satisfy the four requirements of the traditional relief provision of section 66(c) as to W's sole proprietorship income. The IRS further determines that, under the equitable relief provision of section 66(c), it is not inequitable to hold H liable for the sole proprietorship income. Relief is applicable on an item-by-item basis. Thus, H is liable for the tax on half of his wage income in the amount of \$28,000, half of W's wage income in the amount of \$23,000, half of W's sole proprietorship income in the amount of \$17,000, but none of W's investment income, for which H obtained relief under section 66(c). W is liable for the tax on half of H's wage income in the amount of \$28,000, half of W's wage income in the amount of \$23,000, half of W's sole proprietorship income in the amount of \$17,000, and all of W's investment income in the amount of \$5,000, because H obtained relief under section 66(c).

*Example 2. Benefit.* H and W are married, living together, and domiciled in State B (a community property state). Neither H nor W files a return for taxable year 2000. H earns \$60,000 in 2000, which he deposits in a joint account. H and W pay the mortgage payment, household bills, and other family expenses out of the joint account. W earns \$20,000 in 2000. W uses a portion of the \$20,000 to make monthly loan payments on the family cars, but loses the remainder at the local racetrack. In 2002, the IRS audits H and W. H requests relief under section 66(c), stating that he did not know or have reason to know of W's additional income, as H travels extensively while W handles the family finances. Regardless of whether H had knowledge or reason to know of the source of W's income, H is not eligible for traditional relief under section 66(c) because

H benefitted from W's income. H's benefit, the portion of W's income used to make monthly payments on the car loans, was more than a *de minimis* amount. While this benefit was not in excess of normal support, it is enough to preclude relief under the traditional relief provision of section 66(c). H may still qualify for equitable relief under section 66(c), depending on all of the facts and circumstances.

(f) *Fraudulent scheme.* If the Secretary establishes that a spouse transferred assets to his or her spouse as part of a fraudulent scheme, relief is not available under this section. For purposes of this section, a fraudulent scheme includes a scheme to defraud the Secretary or another third party, such as a creditor, ex-spouse, or business partner.

(g) *Definitions—(1) Requesting spouse.* A requesting spouse is an individual who does not file a joint Federal income tax return with the nonrequesting spouse for the taxable year in question, and who requests relief from the Federal income tax liability resulting from the operation of community property law under this section for the portion of the liability arising from his or her share of community income for such taxable year.

(2) *Nonrequesting spouse.* A nonrequesting spouse is the individual to whom the requesting spouse was married and whose income or deduction gave rise to the tax liability from which the requesting spouse seeks relief in whole or in part.

(h) *Effect of prior closing agreement or offer in compromise.* A requesting spouse is not entitled to relief from the Federal income tax liability resulting from the operation of community property law under section 66 for any taxable year for which the requesting spouse has entered into a closing agreement (other than an agreement pursuant to section 6224(c) relating to partnership items) with the Secretary that disposes of the same liability that is the subject of the request for relief. In addition, a requesting spouse is not entitled to relief from the Federal income tax liability resulting from the operation of community property law under section 66 for any taxable year for which the requesting spouse has entered into an offer in compromise with the Secretary. For rules relating to the effect of closing agreements and offers in compromise, see sections 7121 and 7122, and the regulations thereunder.

(i) [Reserved]

(j) *Time and manner for requesting relief—(1) Requesting relief.* To request relief from the Federal income tax liability resulting from the operation of

community property law under this section, a requesting spouse must file, within the time period prescribed in paragraph (j)(2) of this section, Form 8857, "Request for Innocent Spouse Relief" (or other specified form), or other written request, signed under penalties of perjury, stating why relief is appropriate. The requesting spouse must include the nonrequesting spouse's name and taxpayer identification number in the written request. The requesting spouse must also comply with the Secretary's reasonable requests for information that will assist the Secretary in identifying and locating the nonrequesting spouse.

(2) *Time period for filing a request for relief*—(i) *Traditional relief.* The earliest time for submitting a request for relief from the Federal income tax liability resulting from the operation of community property law under paragraph (a) of this section, for an amount underreported on, or omitted from, the requesting spouse's separate return, is the date the requesting spouse receives notification of an audit or a letter or notice from the IRS stating that there may be an outstanding liability with regard to that year (as described in paragraph (j)(2)(iii) of this section). The latest time for requesting relief under paragraph (a) of this section is 6 months before the expiration of the period of limitations on assessment, including extensions, against the nonrequesting spouse for the taxable year that is the subject of the request for relief, unless the examination of the requesting spouse's return commences during that 6-month period. If the examination of the requesting spouse's return commences during that 6-month period, the latest time for requesting relief under paragraph (a) of this section is 30 days after the commencement of the examination.

(ii) *Equitable relief.* The earliest time for submitting a request for relief from the Federal income tax liability resulting from the operation of community property law under paragraph (b) of this section is the date the requesting spouse receives notification of an audit or a letter or notice from the IRS stating that there may be an outstanding liability with regard to that year (as described in paragraph (j)(2)(iii) of this section). A request for equitable relief from the Federal income tax liability resulting from the operation of community property law under paragraph (b) of this section for a liability that is properly reported but unpaid is properly submitted with the requesting spouse's individual Federal income tax return, or

after the requesting spouse's individual Federal income tax return is filed.

(iii) *Premature requests for relief.* The Secretary will not consider a premature request for relief under this section. The notices or letters referenced in this paragraph (j)(2) do not include notices issued pursuant to section 6223 relating to TEFRA partnership proceedings. These notices or letters include notices of computational adjustment to a partner or partner's spouse (Notice of Income Tax Examination Changes) that reflect a computation of the liability attributable to partnership items of the partner or the partner's spouse.

(k) *Nonrequesting spouse's notice and opportunity to participate in administrative proceedings*—(1) *In general.* When the Secretary receives a request for relief from the Federal income tax liability resulting from the operation of community property law under this section, the Secretary must send a notice to the nonrequesting spouse's last known address that informs the nonrequesting spouse of the requesting spouse's request for relief. The notice must provide the nonrequesting spouse with an opportunity to submit any information for consideration in determining whether to grant the requesting spouse relief from the Federal income tax liability resulting from the operation of community property law. The Secretary will share with each spouse the information submitted by the other spouse, unless the Secretary determines that the sharing of this information will impair tax administration.

(2) *Information submitted.* The Secretary will consider all of the information (as relevant to the particular relief provision) that the nonrequesting spouse submits in determining whether to grant relief from the Federal income tax liability resulting from the operation of community property law under this section.

**§ 1.66-5 Effective date.**

Sections 1.66-1 through 1.66-4 are applicable on July 10, 2003. In addition, § 1.66-4 applies to any request for relief filed prior to July 10, 2003, for which the Internal Revenue Service has not issued a preliminary determination as of July 10, 2003.

**PART 602—OMB CONTROL NUMBERS UNDER THE PAPERWORK REDUCTION ACT**

■ **Par. 3.** The authority citation for part 602 continues to read as follows:

**Authority:** 26 U.S.C. 7805.

■ **Par. 4.** The following entry is added in numerical order to the table:

**§ 602.101 OMB Control numbers.**

\* \* \* \* \*  
(b) \* \* \*

CFR part or section where identified and described	Current OMB control No.
* * * * *	*
1.66-4 .....	1545-1770
* * * * *	*

**David A. Mader,**  
*Assistant Deputy Commissioner of Internal Revenue.*

Approved: July 1, 2003.

**Gregory F. Jenner,**  
*Deputy Assistant Secretary of the Treasury.*  
[FR Doc. 03-17386 Filed 7-9-03; 8:45 am]

**BILLING CODE 4830-01-P**

**DEPARTMENT OF THE TREASURY**

**Internal Revenue Service**

**26 CFR Part 301**

[TD 9073]

**RIN 1545-BB17**

**Disclosure of Return Information by Certain Officers and Employees for Investigative Purposes**

**AGENCY:** Internal Revenue Service (IRS), Treasury.

**ACTION:** Temporary regulations and removal of final regulations.

**SUMMARY:** This document contains temporary regulations relating to the disclosure of return information pursuant to section 6103(k)(6) of the Internal Revenue Code. The temporary regulations describe the circumstances under which officers or employees of the IRS, the IRS Office of Chief Counsel, and the Office of Treasury Inspector General for Tax Administration (TIGTA), in connection with official duties relating to any examination, administrative appeal, collection activity, administrative, civil, or criminal investigation, enforcement activity, ruling, negotiated agreement, prefiling activity, or other proceeding or offense under the internal revenue laws or related statutes, or in preparation for any proceeding described in section 6103(h)(2) (or investigation which may result in such a proceeding), may disclose return information to the extent necessary to obtain information relating to such official duties or to accomplish properly any activity connected with