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Income Tax Liability - Liability of Wife for Income Tax Debt - Renunciation of Community Property

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RECENT CASES

INCOME TAX LIABILITY—LIABILITY OF WIFE FOR INCOME TAX DEBT—RENUNCIATION OF COMMUNITY PROPERTY—Commissioner assessed tax liability to Appellant for income taxes due for the years 1955 through 1959. Mrs. Mitchell claimed, because she had renounced her community property rights as provided for by Louisiana law, that she was not liable for the delinquent taxes; and that property inherited by her since the dissolution of the community could not be used by the Commissioner to satisfy the tax debt of the community. The Tax Court of the United States held the wife liable and she appealed. The United States Court of Appeals, Fifth Circuit, reversed holding that the community itself, not the wife as an individual, was liable for the tax and therefore property inherited by the wife after dissolution of the community could not be attached to satisfy the tax debt of the community. *Mitchell v. Comm'r of Internal Revenue*, 430 F.2d 1 (5th Cir. 1970).

Taxpayer was married in 1946 and during the years in question lived in the state of Louisiana, a community property state. The Tax Court found as a matter of fact that Mrs. Mitchell did not know of her husband's finances and relied upon his assurances that their tax returns were properly paid for the years in question.[1] In July, 1960, Mrs. Mitchell and her husband were separated. In 1961, taxes were assessed against the Mitchells, but Mrs. Mitchell had no knowledge of this assessment. Fourteen days after this assessment Mrs. Mitchell renounced her community interests in her marriage pursuant to Louisiana law.[2] In October of 1962, the Mitchells were divorced. In 1964, Mrs. Mitchell inherited property from her mother's estate and shortly thereafter transferred her interest therein to her sister without consideration.

The Tax Court based its decision upon its belief that Section 2410 of the Louisiana Code only permits the wife to exonerate herself from the contractual obligations of the marriage and that

1. Mitchell v. C.I.R., 51 T.C. 641, 642-643 (1969).
2. "Both the wife and her heirs or assigns have the privilege of being able to exonerate themselves from the debts contracted during the marriage, by denouncing the partnership or community of gains." LOUISIANA STAT. ANN. § 2410 (1952).

since taxes are an obligation imposed by the law, renunciation had no effect upon her liability from taxes imposed upon the community income.[3]

In reversing the decision of the Tax Court, the Court of Appeals focused upon the fact that:

> [U]nder Louisiana law the wife has a present, vested ownership interest in one-half of the community property, including its income.[4]

However, the court went on to say,

> [T]he bare characterization of this ownership interest as vested is not determinative of the issue. Under the law of Louisiana, the wife does not own the income in a separate capacity. She owns the income only derivatively through her one-half ownership interest in the community. It is the community which owns the income and owes the community debts.[5]

From the conclusion that the community owns the income, the court reasoned that, according to *Helvering v. Horst*,[6] the community, not the wife, owes the tax.

In 1930 the Supreme Court, in a series of cases determined that a husband and wife in the community property states of Washington,[7] Arizona,[8] Texas,[9] and Louisiana[10] could properly split their income and file separate returns, each claiming one half the income of the community for the year. These decisions were based upon the determination by the Court that the interest of the wife in the income was vested and as a present property interest could properly be attributable to her as *her* income.[11]

In reaching its decision in the instant case, the Court of Appeals relied upon *Pfaff* for the proposition that it is the community which owns the income (although conceding that the wife has a vested interest therein) and therefore it is the community which owes the "debt". It is interesting to note at this point that the

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3. Mitchell v. Comm'r., 51 T.C. 641, 646 (1969); *citing* Bender v. Pfaff, 38 F.2d 649 (5th Cir. 1930); *aff'd* Bender v. Pfaff, 282 U.S. 127 (1930).
4. Mitchell v. C.I.R., 430 F.2d 1, 4 (1970); *citing* United States Fidelity and Guarantee Co. v. Green, 252 La. 227, 210 So.2d 328 (1968); and, Phillips v. Phillips, 169 La. 813, 107 So. 584 (1926).
5. Mitchell v. C.I.R., 430 F.2d 1, 4 (1970); *citing* Poe v. Seaborn, 282 U.S. 101 (1930); and Bender v. Pfaff, 38 F.2d 649 (5th Cir. 1930); *aff'd* Bender v. Pfaff, 282 U.S. 127 (1930).
6. *See* Helvering v. Horst, 311 U.S. 112 (1940).
7. Poe v. Seaborn, 282 U.S. 101 (1930).
8. Goodell v. Koch, 282 U.S. 118 (1930)
9. Hopkins v. Bacon, 282 U.S. 122 (1930).
10. Bender v. Pfaff, 282 U.S. 127 (1930).
11. This disparity between community property and common law states has subsequently been remedied by 26 U.S.C. § 6013.

Tax Court relied on *Pfaff* and its companion case of *Poe v. Seaborn*[12] to reach the opposite conclusion and find that Mrs. Mitchell was liable for the tax "debt." They concluded:

> We find no reason why the constitutional precepts *Poe v. Seaborn*, that were applicable in permitting community income to be split, should not be applicable in requiring the spouse to report and pay her tax on one-half of the community income.[13]

It is submitted that the opinion of the Tax Court is a better reasoned opinion and more in keeping with the existing system of income taxing. The Tax Court pointed out in its opinion, that the tax liabilities involved were not a "debt" as envisioned by Section 2410 of the Louisiana Code.[14] Also, the Court pointed out that taxpayer had renounced her community property interest after her tax liability had arisen.[15]

Further, the Court pointed out that a wife in Louisiana is not at liberty to assume or refuse to assume the tax liability of the community,[16] yet the Appellate Court provides her this opportunity by making her renunciation of the Community interest effective to relieve her of tax liabilities already attached. In so doing, the Court of Appeals cites *Messersmith v. Messersmith*[17] for the proposition that "[A]ll sums expended for income tax . . . must be held to be debts of the community and to be payable out of community funds."[18] However, upon closer reading, it is readily apparent that the court in *Messersmith* states a proposition different from that cited by the Court in *Mitchell*. The passage quoted from *Messersmith* reads in full,

> [A]ll sums expended for income tax *prior to the rendition of judgment of separation from bed and board, March* 25, 1949, must be held to be debts of the community and to be payable out community funds.[19] (Emphasis added)

Consequently, even if it is conceded that taxes are "debts" as envisioned by Section 2410 of the Louisiana Code and therefore subject to renunciation, Louisiana law properly construed holds

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12. Poe v. Seaborn, 282 U.S. 101 (1930).
13. Mitchell v. Comm'r., 51 T.C. 641, 647 (1969).
14. *Id.* at 646. Here again the *Pfaff* decision was relied upon. In the Circuit Court decision rendered in *Pfaff* the court stated, "[A] tax is not a debt created by contract. It is created by law, and a duty exists to pay it." Bender v. Pfaff, 35 F.2d 649, 651 (1930). This decision was later affirmed by the Supreme Court as noted *supra*, and no mention was ever made of the tax obligation being a "debt" as envisioned by § 2410 of the Louisiana Code.
15. Mitchell v. Comm'r., 51 T.C. 641, 648 (1969).
16. *Id. citing* Smith v. Connelly, 65 F.Supp. 415, 417 (E.D. La. 1946); Saenger v. Comm'r., 69 F.2d 633 (5th Cir. 1934); Comm'r. v. Hyman, 135 F.2d 49 (5th Cir. 1943).
17. Messersmith v. Messersmith, 229 La. 495, 86 So.2d 169 (1956).
18. *Id.* at 176, as cited in Mitchell v. C.I.R., 430 F.2d 1, 4.
19. *Id.* at 176.

only that "sums expended for income tax prior to the rendition of judgment of separation from bed and board" are "debts" which may be renounced. These "debts" were attached prior to separation, but payment was not sought by the Commissioner until after separation. Therefore they do not fit the definition of "debts" laid down in *Messersmith* and relied upon by the Court as a construction of Section 2410 of the Louisiana Code.

The second criticism of the Appellate Court's decision is its limited reading of *Pfaff* and subsequent cases. In its opinion the Tax Court pointed out that while *Pfaff* and its companion cases held that income could be split between husband and wife when reporting income, such income splitting was not mandatory. However, in the case of *Paul Cavanaugh*[20] it was held that the wife was obligated to return one-half of the income of the property. The Tax Court stated in *Cavanaugh*:

> [I]ncome must be reported by the individual to whom the statute attributes it. Clearly, therefor, the petitioner's wife is taxable on one-half of the community income. She is the owner thereof, although not entitled to present possession. . . .
>
> Consequently, there is no longer the situation whereunder the wife may at her option return one-half of the income.[21]

Citing the *Pfaff* line of cases and *United States v. Malcolm*,[22] the Court of Appeals for the 9th Circuit upheld the Cavanaugh decision that income admittedly earned by the husband alone (the wife was residing in Canada during the taxable period in question) was taxable to him only to the extent of his one-half interest in the community. The other income was taxable to his wife.[23]

In the *Malcolm* case the Supreme Court held that the entire income tax in California is not due from the husband, but rather it is community income, and that a wife in California is obligatd to report and pay tax on one half of the community income.[24] It is worthy of note that the Supreme Court cited the *Pfaff* line of cases as authority for its decision in *Malcolm*. The Court of Appeals in the instant case ignores this mandatory splitting interpretation of *Pfaff* and says instead that the *Pfaff* decision merely permits income splitting if the wife so chooses, but if she chooses not to claim one-half of the community income as earned by her,

20. Paul Cavanaugh, 42 B.T.A. 1037 (1940); *aff'd* 125 F.2d 366 (9th Cir. 1942).
21. *Id.* at 1043-1044.
22. United States v. Malcolm, 282 U.S. 792 (1931).
23. C.I.R. v. Cavanaugh, 125 F.2d 366 (1942).
24. United States v. Malcolm, 282 U.S. 792, 793 (1931).

the husband is powerless to compel her to do so. In view of the one paragraph opinion in *Malcolm*, the Supreme Court does not agree.

It is submitted that the decision rendered in this case may prove to be unworkable and that it results in an inequity to the husband in a community property state. Perhaps the Louisiana Code is the source of inequity with its provision for renunciation by a wife, but none for a husband (although, as discussed above, Section 2410 of the Code is open to an interpretation other than the unjust one applied here).

One wonders whether the Court of Appeals would have been so willing to allow the taxpayer to escape liability if it had been the husband who sought to renounce his community interest and thereby have all the income assessed to his wife. In a time when the law is ever more watchful of women's rights under the guise of "women's lib," perhaps it should also consider declaring unconstitutional such archaic laws as Section 2410 of the Louisiana Code, or courts should at least avoid interpretations of laws which will afford special privileges to women merely because they are women. After all, equality is a double-edged sword; we must be careful that women be equal to men, but also careful that they aren't made, by decisions such as this, *more* equal than men.

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SELECTIVE SERVICE ACT—ARMED SERVICES—REOPENING I-S(C) CLASSIFICATION—While not enrolled at a university, plaintiff was ordered to report for induction. Prior to the date of his scheduled induction, he voluntarily enrolled at a university, notified his local draft board of his new student status, and requested to be reclassified from I-A to I-S(c). The local board refused to reopen his classification stating that the facts presented were not sufficient to qualify him for a I-S(c) deferment since they did not show that he was satisfactorily pursuing a full-time course of instruction on the date of receipt of his induction order. Thereafter, plaintiff sought an injunction from the United States District Court, to enjoin the local board from inducting him.

In declining jurisdiction and at the same time deciding the merits of the case the court held that the failure of the local board to reopen plaintiff's I-A classification when informed of his new status was not "blatantly lawless"[1] because the board

1. 50 U.S.C.A. App. § 460(b)(3) (1967) states: "No judicial review shall be made