

STATE OF NEW YORK

DIVISION OF TAX APPEALS

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In the Matter of the Petition	:	
of	:	
<b>DARIA CARNESI</b>	:	<b>DETERMINATION</b>
	:	<b>DTA NO. 823507</b>
for Redetermination of a Deficiency or for Refund of	:	
Personal Income Tax under Article 22 of the Tax Law	:	
for the Years 1992 through 1995.	:	

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Petitioner Daria Carnesi filed a petition for redetermination of a deficiency or for refund of personal income tax under Article 22 of the Tax Law for the years 1992 through 1995.

A hearing was held before Thomas C. Sacca, Administrative Law Judge, at the offices of the Division of Tax Appeals, Empire State Plaza, Agency Building 1, Albany, New York 12223, on February 24, 2012 at 10:00 A.M., with all briefs to be submitted by August 20, 2012, which date began the six-month period for the issuance of this determination. Petitioner appeared by Michael H. Stephens, Esq. The Division of Taxation appeared by Mark F. Volk, Esq. (Christopher O'Brien, Esq., of counsel).

***ISSUE***

Whether petitioner Daria Carnesi is entitled to relief from New York State personal income tax for the years 1992 through 1995 as an innocent spouse pursuant to Tax Law § 651(b)(former [5][A]).

***FINDINGS OF FACT***

1. Following an audit, the Division of Taxation (Division) issued to petitioner Daria Carnesi and her husband Kenneth Carnesi a Notice of Deficiency, dated September 29, 1997, that assessed personal income tax due of \$96,389.76, plus penalty and interest, for the years 1992 through 1995.

2. During the audit period Kenneth Carnesi was an attorney, practicing as a sole practitioner under the name Carnesi & Associates. He also operated a consulting firm entitled Banfinanz, Ltd., that was involved in advising European companies on the methods available to obtain financing from American banking institutions. Banfinanz, Ltd., was a subchapter S corporation wholly owned by Mr. Carnesi. Associated with his law practice and consulting firm were various expenses he incurred during the years of the audit, including expenses for personnel, the lease of the building where he operated his law practice and consulting firm, utilities and health care costs.

3. On February 11 and 13, 1997, an auditor from the Division telephoned Kenneth Carnesi for the purpose of informing him that an audit of his consulting business and legal practice was to be conducted for the years 1992 through 1995. On both occasions the auditor left a message for Mr. Carnesi to contact the auditor. No return telephone call was made by Mr. Carnesi to the auditor.

4. On March 10, 1997, the auditor sent a letter to Mr. Carnesi advising him of the audit and stating that an appointment had been scheduled for April 3, 1997 at the Division's offices. Mr. Carnesi did not appear at the scheduled appointment. The auditor telephoned and again left a message for Mr. Carnesi on April 7, 1997 to telephone the auditor. Mr. Carnesi again did not respond to the message. On April 22, 1997, the auditor sent proposed audit adjustments to

Kenneth and Daria Carnesi at their home address for the years 1992 through 1995. The cover letter accompanying the computations provided Mr. and Mrs. Carnesi with the opportunity to discuss the audit findings in detail, and requested that they telephone the Division's office by May 12, 1997. No telephone call was received by the Division's office. On May 22, 1997 and June 27, 1997, two additional messages were left at Mr. Carnesi's office by the auditor, without response.

5. The basis of the proposed audit adjustments and subsequent notice of deficiency was the disallowance of all Schedule C claimed expenses for Mr. Carnesi's law practice and consulting firm and the disallowance of all itemized deductions claimed by Mr. and Mrs. Carnesi on their joint returns for the years 1992, 1993 and 1994. The personal income tax returns for these three years were all dated April 12, 1996 and received by the Division on April 30, 1996. As no return was filed for the year 1995, the auditor estimated income based upon the actual reported 1994 income appearing on Mr. and Mrs. Carnesi's personal income tax return for that year.

6. Due to the failure of Kenneth and Daria Carnesi to timely protest the notice of deficiency, the Division issued, on January 22, 1998, a notice and demand for the tax, penalty and interest due as determined on audit. Thereafter, a warrant was docketed on November 23, 1998 against petitioner and her husband. A lien was placed on their home, and following a sale of the house as a result of a mortgage foreclosure in March 2005, payment was made to the Division on November 13, 2006 in the amount of \$338,852.28. In addition, petitioner's wages were garnished in the amount of \$6,240.00 and the Division took possession of their son's Uniform Transfers to Minors Act (UTMA) custodial account in the amount of \$5,279.00.

7. Petitioner filed a request for a conciliation conference on October 9, 2007 seeking a refund of one-half of the proceeds from the foreclosure sale, or \$169,426.14, together with a return of her wages garnished in the amount of \$6,240.00, on the basis that she is entitled to innocent spouse status. The Division stipulated at hearing to refund the money seized from the UTMA custodial account in the amount of \$5,279.00.

8. Petitioner obtained a B.A. degree from C.W. Post University in 1978 and a paralegal certificate from Adelphi University in the same year. She was employed by New York Life Insurance Company as a contract analyst until 1985, when she left employment to stay at home maintaining the couple's household and caring for their two young children. She did not work outside the home again until 2005.

9. During the years at issue, petitioner was not involved in the payment of the household expenses, except for groceries, clothes for the children and other basic necessities. Mr. Carnesi would give petitioner approximately \$300.00 to \$350.00 each week to cover these expenses. All other family expenses, such as the mortgage, utilities, automobile and medical insurance and the leases on the automobiles were paid by Mr. Carnesi. Petitioner was unaware as to how these bills were paid, from what account they were paid or whether Mr. Carnesi had a personal account. Petitioner was certain that she did not have a joint bank account with her husband. Finally, petitioner took no role in Mr. Carnesi's law practice or consulting firm.

10. Petitioner was not involved in the preparation of the joint personal income tax returns filed by the couple for the years 1992, 1993 and 1994. Mr. Carnesi prepared the returns, and with petitioner's consent, signed petitioner's name to the returns. Petitioner never reviewed the returns, or inquired as to the contents of the returns. Mr. Carnesi considered the itemized deductions and business expenses claimed on the personal income tax returns to be appropriate.

It was his opinion that at the time the returns were filed, sufficient documentation existed to substantiate the deductions shown on the returns.

11. There was no dramatic change in the couple's lifestyle during the years at issue. There were no structural additions to the family home, they did not take vacations or entertain on a large scale. Petitioner mowed the lawn, did much of the landscaping and shoveled the snow in the winter.

### ***CONCLUSIONS OF LAW***

A. Tax Law § 651(b) (former [5][A]), in effect during the years at issue, provided that if:

- (i) a joint return has been made under this subsection for a taxable year,
- (ii) on such return there is a substantial understatement of tax attributable to grossly erroneous items of one spouse,
- (iii) the other spouse establishes that in signing the return he or she did not know, and had no reason to know, that there was such substantial understatement, and
- (iv) taking into account all the facts and circumstances, it is inequitable to hold the other spouse liable for the deficiency in tax for such taxable year attributable to such substantial understatement, then the other spouse shall be relieved of liability for tax (including interest, penalties and other amounts) for such taxable year to the extent that such liability is attributable to such substantial understatement.

For purposes of this statute, the term "grossly erroneous items" means:

any item of New York adjusted gross income attributable to such spouse which is omitted from New York adjusted gross income and any claim of a New York deduction, exemption, credit or basis by such spouse in an amount for which there is no basis in fact or law. . . (Tax Law § 651[b][former (5)(B)(i)]).

The term "substantial understatement" means any understatement which exceeds one hundred dollars (Tax Law § 651[b][former(5)(B)(ii)]).

B. As the wording of this provision is almost identical to its parallel provision in the Internal Revenue Code, (*see* 26 USC § former 6013[e][1]), it is appropriate to refer to the provisions of the Internal Revenue Code, Treasury Regulations and federal and New York case law to determine petitioner's eligibility for innocent spouse relief (*see* Tax Law § 607[a]). An individual claiming innocent spouse status in an erroneously claimed deduction case must establish that a joint return was filed, on the return there is a substantial understatement of tax attributable to grossly erroneous items of one spouse and at the time the joint return was signed, the other spouse did not know, and had no reason to know, that the deductions in question would give rise to a substantial understatement of tax on the joint return (*Reser v. Commissioner*, 112 F2d 1258 [1997]).

C. Petitioner and Kenneth Carnesi did not file a return for the year 1995, and therefore petitioner is not entitled to innocent spouse relief for this year (Tax Law § 651[b] [former (5)(A)(i)]; *Shea v. Commissioner*, 780 F2d 561 [1986]).

D. Since petitioner and Kenneth Carnesi did file joint returns for the years 1992, 1993 and 1994, the first criterion for innocent spouse status has been satisfied for these years. In addition, it is clear from the amount of the deficiencies that there was a substantial understatement of tax for each of the years. However, the substantial understatement cannot be found to have been attributable to grossly erroneous items of one spouse.

If the allegedly erroneous items had a factual or legal basis, that is, petitioner and Mr. Carnesi claimed the deductions on the premise they were entitled to such deductions, innocent spouse relief is not available (*Purcell v. Commissioner*, 826 F2d 470 [1987], *cert denied* 485 US 987 [1988]), since the understatement cannot be found to have been attributable to grossly erroneous items. Here, petitioner made no showing that the itemized and business deductions

that were disallowed lacked a basis in fact or law. The record in this matter only establishes that the couple did not substantiate the claimed deductions. In fact, the documentation and testimony in the record with respect to these items indicate that the couple considered the deductions proper, being based on expenses relating to their home and Mr. Carnesi's law practice and consulting firm. Both petitioner and Mr. Carnesi testified that had they been aware of the audit and its basis, they would have been able to document most, if not all, of the deductions claimed. Petitioner testified that she was unaware of the audit, the issuance of the statement of audit changes, the notice of deficiency, the notice and demand, the request and docketing of the warrant and the numerous telephone calls of the auditor. According to petitioner, it was not until the mortgage foreclosure action and payment of the deficiency from the proceeds that she became aware that an audit had been conducted and an assessment had been issued. Mr. Carnesi testified that, except for a brief meeting with the auditor concerning his consulting firm, he only became aware of the audit and its results when he discovered in late 2001 that a tax warrant had been filed. Such testimony concerning petitioner's and Mr. Carnesi's lack of knowledge regarding the audit and subsequent collection actions lacks credibility, given the numerous letters and telephone calls to both Mr. Carnesi's business location and the couple's home, as well as the numerous legal actions taken to collect the debt, and directly conflicts with petitioner's own allegations both pre- and post-hearing that Mr. Carnesi had intercepted all the mail from the Division concerning the audit and subsequent collection action. In short, the testimony claiming that the deductions were proper negates petitioner's position that the understatement was "attributable to grossly erroneous items of one spouse." The joint returns filed by petitioner and her husband set forth the premise that they were properly entitled to the claimed deductions, and

they both claimed the same premise in their respective testimony. Thus, the filings had a factual or legal basis and petitioner is not entitled to innocent spouse relief (*Purcell v. Commissioner*).

In light of the above, it is determined that petitioner has failed to meet the requirement that there was a substantial understatement of tax attributable to grossly erroneous items of one spouse.

E. In addition, petitioner has also failed to show that she did not know, and had no reason to know, that the returns for the years 1992, 1993 and 1994 contained substantial understatements. Petitioner testified that she was not involved in the preparation of the joint personal income tax returns filed by the couple for the years 1992, 1993 and 1994. Mr. Carnesi prepared the returns, and with petitioner's consent, signed petitioner's name to the returns. Petitioner never reviewed the returns, or inquired as to the contents of the returns. Petitioner admitted that she was unaware as to how monthly bills were paid, from what account they were paid or whether Mr. Carnesi had a personal account. The handling of all financial matters, including the preparation of tax returns was left to and was the responsibility of Mr. Carnesi. Petitioner's admissions, even if credible, are insufficient to sever her liability for the tax due in this matter.

In order to be accorded innocent spouse status, the statute provided that in signing the return, the other spouse (in this case, petitioner) "did not know, and had no reason to know, that there was such substantial understatement . . ." (Tax Law § 651[b][former (5)(A)(iii)]). Clearly, Mrs. Carnesi was an educated woman. She had a bachelor's degree and a paralegal certificate. Petitioner was a former contract analyst with a large insurance company. Had this been a case where Mr. Carnesi claimed an exemption or deduction to which he was not entitled, or concealed some income of which Mrs. Carnesi was unaware, then perhaps it could be found that



she “had no reason to know” of the resulting substantial understatement. The claimed business and itemized deductions were clearly listed on the returns filed and petitioner chose to intentionally insulate herself from the process of preparing, reviewing and signing the returns. There is no evidence that Mr. Carnesi ever attempted to conceal any additional income; the deductions were plainly designated on the joint returns. A spouse’s role as a homemaker, giving complete deference to the other spouse’s judgment concerning the couple’s finances, standing alone, is insufficient to establish that a spouse has no “reason to know” (*Resser v. Commissioner*, 74 F3d 1536 [1996]). Furthermore, an innocent spouse is one who despite having made reasonable efforts to investigate the accuracy of the joint return remains ignorant of its illegitimacy (*Matter of Revere v. Tax Appeals Tribunal*, 75 AD3d 860, 907 NYS2d 326 [2010]). Here, petitioner made no effort to ascertain the accuracy of the joint returns.

F. The cases cited by petitioner in support of her position are distinguishable from the present matter. In *Hinds v. Commissioner*, (56 TCM 104[1988]), the court found that the wife was entitled to innocent spouse relief. However, the wife was led to believe that the returns were prepared by certified public accountants, the couple had a “fragile and strained” relationship due to the abusive conduct of the husband, and the wife lacked any business knowledge or experience. These factors are not present in this matter. In *Price v. Commissioner* (887 F2d 959 [1989]), the court also found that the wife was entitled to innocent spouse relief. However, the husband had led his wife to believe that the returns were prepared by certified public accountants. In addition, when the wife reviewed the returns and raised her concerns about a large, unsubstantiated deduction, the husband assured her that the accountants would not have allowed it were it not legal. Unlike the present matter, the factual circumstances in *Price* involved a

spouse who reviewed the returns, questioned a deduction and was deceived by her husband at the time the returns were filed.

G. Petitioner has failed to meet the requirement that she did not know or have reason to know of the understatements contained in the income tax returns filed for the years 1992, 1993 and 1994. (*Matter of Revere v. Tax Appeals Tribunal*, [where a spouse was not relieved of his liability where he intentionally remained ignorant regarding the preparation of his joint tax returns because he did not want to get involved]; *Matter of Rubin v. Tax Appeals Tribunal*, 29 AD3d 1089, 814 NYS2d 804 [2006][where a spouse was not relieved of her liability despite her claim that she had never been involved in the financial aspects of the marriage and relied on her husband and the professionals he retained to accurately prepare the tax returns, and there was no evidence that the husband had ever tried to conceal the excluded income].)

H. By virtue of the determination that petitioner has failed to meet the requirements of Tax Law § 651(b)(former [5][A][i],[ii]), it is hereby found that petitioner is not entitled to innocent spouse status.

I. As stipulated by the Division (*see* Finding of Fact 7) petitioner is entitled to a refund in the amount of \$5,279.00 representing the money taken from her son's UTMA custodial account.

J. The petition of Daria Carnesi is granted to the extent indicated in Conclusion of Law I and the Division of Taxation is directed to refund the amount of \$5,279.00, plus appropriate interest thereon. In all other respects the petition is denied.

DATED: Albany, New York  
December 6, 2012

/s/ Thomas C. Sacca  
ADMINISTRATIVE LAW JUDGE