



Lowenstein Sandler's Trusts & Estates Podcast: Splitting Heirs

Episode 13:
The Divorce, the Innocent Spouse, and the \$78,000 Mercedes

By [Warren K. Racusin](#), [Elie Honig](#), [Melissa Wiley](#)
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Kevin Iredell: Welcome to the Lowenstein Sandler podcast series. I'm Kevin Iredell, Chief Marketing Officer at Lowenstein Sandler. Before we begin, please take a moment to subscribe to our podcast series at lowenstein.com/podcasts. Or find us on Amazon Music, Apple Podcasts, Audible, iHeartRadio, Spotify, Soundcloud or YouTube. Now let's take a listen.

Warren Racusin: From the law firm, Lowenstein Sandler, this is Splitting Heirs. I'm Warren Racusin. Our devoted S Silent H listeners know that we build each episode around a real client story, changing the facts just enough to protect the innocent, or the guilty, depending on how you look at it. We say like they do in the movies, our episodes are inspired by true events. Well, this time we take it to the next level. Talk about a real live case in the United States Tax Court, not one of ours. It involves an interesting couple doing some sketchy things on their tax returns, getting caught by the tax man or the tax woman, and one spouse wriggles out of the marriage and tries to wriggle out of the tax. Like all of our episodes, we hope it's just the right mix of information and entertainment.

Warren Racusin: Now to unpack all this, we've got my partner Melissa Wiley, who's in our Washington DC office and does battle with the IRS on tax cases all the time. And our special guest, CNN's senior legal analyst, former federal prosecutor, and our colleague Elie Honig. Elie, Melissa, great to have you both here. Welcome.

Melissa Wiley: Thank you for having us, Warren.

Elie Honig: Thanks, Warren. I think I need to do a disclaimer up top. I'm not a tax expert, but I'm going to do my best to hang with you guys, and I will I guess later be talking about a case of mine that involved a few tax charges.

Warren Racusin: Well, we always like to have an outside expert with a different focus on things, and that's one of the many reasons that we're really happy that you're here today. So let's dive in. Melissa, since you litigate against our good friends at the IRS all the time. Why don't you lead us off by taking us through the fact of the great case of DeGuzman versus the Commissioner of Internal Revenue?

Melissa Wiley: So Warren, you may also know this, it's a professional liability, but when you tell people that you're a tax lawyer, it tends to stop the conversation. People don't necessarily gather around you. They think it's dull, boring. I like the fact that this podcast has dispelled that notion on your end in the estate planning world, but I also want to do my best to dispel that notion on the straight-up tax world. So I think our DeGuzman case here is a pretty great example of how tax can be just as interesting, salacious, and filled with personality as any other area of boah.

Warren Racusin: We're all about salacious and filled with personalities, so have at it.

Melissa Wiley: All right. Well, the DeGuzmans were at one point a happily married couple. I'm going to set up the true life story made for TV movie. Mrs. DeGuzman was a nurse. Her husband was a surgeon. They fell in love. They adopted four beautiful children. Mrs. DeGuzman decided to stay at home with those children after a while because I can't imagine taking care of four children. Her husband got out of the surgery business, got into the medical device business and was, let's just say very successful ultimately selling and starting a number of companies. One of his sales netted him somewhere between eight and \$10 million. They moved to Arizona and lived the good life. One of the really notable things about this case is that this is a case where the IRS audited our friends, the DeGuzmans. They found hundreds of thousands of dollars of false deductions over each of three tax years, '16, '17, and '18.

At the end of the audit, however, by that point, the DeGuzmans had been divorced. Mrs. DeGuzman invoked a provision of the Internal Revenue Code section 6015 that we generally refer to as innocent spouse relief. Now, innocent spouse relief takes a look at a jointly filed tax return, and for everyone who files one listen up. Innocent spouse relief under the tax code, and it's section 6015 for anyone who wants to look it up if they're having trouble sleeping tonight, provides that if you file a joint tax return and listen up if you do, normally the rules are that you and your spouse are jointly liable for that tax. Now, what does that mean? If you split up from your spouse, if you discover that your spouse is doing some things that you don't really agree with or didn't know about, you are still on the hook for any tax liability that may arise on a jointly filed return.

Well, the DeGuzmans in these years filed those, but at the end of their audit, Ms. DeGuzman said, look, I was not responsible for these amounts. These were amounts that were deducted by my no-good ex-husband. I had no idea. Please, please provide me with what is called innocent status relief. The government surprisingly agreed. They said, that's fine. We're going to pin this all on him. And Mrs. DeGuzman, you are off the hook. Well fast-forward, and sometimes when couples split up, there's some lingering animosity.

Warren Racusin: That does happen I've heard.

Melissa Wiley: Mr. DeGuzman intervenes in the audit and says, "No, no, no. My ex-wife should have to bear half of this. This was a jointly filed return, and she should not qualify for innocent spouse relief." What happens is these three, the IRS, Mr. And Mrs. De Guzman end up in court in the US tax Court in where else? Las Vegas, Nevada. The sitting judge, Judge Toro decided to issue after trial

his opinion orally from the bench and it is a good one. His task was to figure out whether Mrs. DeGuzman should be able to invoke innocent spouse relief and not have to pay her half or whether Dr. DeGuzman was correct, and they should have to split this bill. I'm going to let you guess where the judge turns out just by reading a little bit of what he includes in his opinion. At one point the DeGuzman's employed a housekeeper, a nanny, a chef, and a gardener.

In addition, they had professionals come to their home to provide Mrs. DeGuzman manicures, cut their children's hair, and maintain their pool. They took expensive vacations going skiing in France, dogs sledding in Sweden, and on a safari in Africa among others. Their children attended private school. Mrs. De Guzman bought luxury items such as an Hermes Birkin bag and thousand dollars designer shoes. They borrowed and spent considerable sums of money in an effort to build a second 12,000 square foot, and I quote, "dream home." And this is what really irks the judge. Shortly before trial in March 2023, Mrs. De Guzman traded in a 2018 Mercedes-Benz awarded to her in the divorce. It was valued at \$31,000. She acquired a new Mercedes-Benz costing approximately \$78,000. Meanwhile, the DeGuzmans failed to keep current on their tax obligations. Now, Warren, I'm going to punt it to you here. Where do you think the judge ends up on whether Mrs. DeGuzman should be paying part of this tax liability?

Warren Racusin: Well, one listens to the facts, particularly when you hear the part about the \$78,000 Mercedes and the fact that apparently, Mrs. DeGuzman was involved with the preparation of the tax returns. You would think, just going out on a limb here, that the judge would say, you don't sound so innocent to me.

Melissa Wiley: Now, when we invoke innocent spouse, we typically think of bad marriages occasionally, or actually quite often spouses who have been abused. This doesn't really sound like that, does it?

Elie Honig: Can I jump in with a quick question for you as a lay person?

Melissa Wiley: Yeah.

Elie Honig: What determines if a person, what does it mean to be an innocent spouse? Or does it mean did you spend a lot of money like Ms. De Guzman did or does it mean were you involved somehow in the filing of tax returns, or does it mean something else?

Melissa Wiley: Well, that is a great question. And what the tax code requires for you to be eligible for innocent spouse relief is that the tax that's attributable to the items that cause the adjustment related to the non-claiming spouse. So here it would be that all of the deductions that were denied were allocable to Mr. De Guzman.

Warren Racusin: That they were his deductions, they weren't deductions that she took for anything that she did. So she didn't try to deduct the Birkin bag and she didn't try to deduct the Mercedes, et cetera.

Melissa Wiley: Not that the IRS found out, that is correct. And in this case, the court finds yes, that is exactly what happened. She was not working during these years. She was getting manicures and taking care of the children. So all of the adjustments related to him. The next requirement is that the spouse that is claiming Innocence Spouse relief did not know and had no reason to know that there was an understatement of taxes. Here we're feeling a little bit less confident in Mrs. De Guzman's case. As Warren noted, she was the one who was transmitting all the information to the accountant. She had the court notes, she had a college degree, she was dealing with the tax returns all the time. But this is for me, the real sticking point. The last requirement, Elie, is that it is inequitable to hold the other individual liable for the deficiency.

Warren Racusin: Inequitable.

Melissa Wiley: It is inequitable. So it is inequitable to hold Mrs. DeGuzman individually liable for the deficiency. You read those, and you're not feeling so good about her chances.

Warren Racusin: Maybe how to buy a Bentley instead of a Mercedes.

Melissa Wiley: Well, I have to say, I would have loved to be present for this trial just because of the detail that ends up in this opinion about where they went on their vacations, what bags she was buying, how much her shoes cost. Those are really, really detailed allegations and facts that have to be found by the judge. So there had to be some evidence. But what the judge ends up finding is that the government actually did not do a great job, and there's some dispute of whether it was the government's job or the ex-husband's job because he was intervening of showing that Mrs. DeGuzman knew what was going on when it came to the inflation of the deductions. And that burden actually wasn't met. And because of the fact that they were divorced at the time all of this was happening, it is the burden of the government to show that she knew what was going on and was in on it, and that they just sort of missed the boat there.

Now the government was in a real difficult position here because remember, they agreed during the audit that she should get innocent spouse relief for reasons not in the opinion. So the government doesn't seem to be real motivated to make that proof here, but apparently Dr. DeGuzman who I should note represented himself in this case, another reason that I would've really liked to see this trial, apparently also did a poor version of that. And as someone who has litigated tax cases with couples who, let's just say, are no longer in the honeymoon phase, I can tell you that sometimes they don't really focus on things like the burden of proof so much as getting into the record facts that they decide are really important for everybody to know about their now spouse.

Elie Honig: Melissa, can I throw in a question here? Why does the government, the IRS care? Or do they care? I mean, if they're going to get paid, why do they care if all of it from the husband or 50% is from each side? Do they care? Because what made me think about this is you said it's rare for the government to agree that one spouse should get innocent spouse relief, but would it matter to the government?

Melissa Wiley: From a dollars and cents point, it doesn't matter. From an equity point, it does because when you're asking for innocent spouse relief, what you're doing is asking for the legal allocation of the burden to change. That theoretically when you sign a joint return, you know that you are on the hook for half of whatever that says. And so when you claim innocence fast relief, what you're asking the government to do is override that. And so from an equity perspective, from a perspective of keeping the system working as it should, the government does care. But you're right, from a dollars and cents perspective here, I don't think Dr. DeGuzman was necessarily fired up to be able to pay the tax that was owed.

Elie Honig: Right. I do have to note in every case involving propagate spending or embezzlement or campaign finance violations, there's always something Hermes involved, and I know how to say that word, H-E-R-M-E-S, not because I own anything that's Hermes, but because it comes up in every one of these cases.

Warren Racusin: So Melissa, this wasn't a criminal case. But based on the fact that wouldn't it have been a stretch; it seems to me at least to have made it a criminal case. So let's talk about criminal tax fraud, civil tax fraud, and what are the differences between those? Let's chat about that a little bit just to right set this for everybody.

Melissa Wiley: Sure thing. So among the monopoly of penalties the IRS can impose when they find that a taxpayer has done something they shouldn't have done are fraud penalties. On the civil side, those are strictly imposed as penalties. They are a percentage of the tax that is found to have been evaded. On the criminal side, as is the case in most crimes when there's both the criminal and civil component, there are fines that do not necessarily correspond to the tax that was evaded but are meant to punish and also potential criminal crime.

Warren Racusin: So as I tell our clients, civil tax fraud means you did something bad, and you got to pay us a bunch of penalties. Criminal tax fraud means you got to pay penalties, and we have to go to the hoosegow as well. Or as I always explain to clients when we're doing estate tax returns and they say, "Well, do we have to report all of the artwork and the jewelry in the house?" And I say, "Listen, filing or assisting in the filing of a false tax return is a felony punishable by fine and imprisonment." And that usually gets their attention.

Melissa Wiley: It does usually get their attention. Criminal fraud is usually handled by the IRS criminal investigative division, so CI or CID, for those of us who have been practicing a long time. When you heard about the IRF getting more money and there're being 80,000 new agents with guns, these are the people actually that hold the guns in the IRS. They're the only people that hold the guns in the IRS, and there are not a ton of them, a few thousand. In fiscal 2023, there were about 21, 2200 special agents. But these are really highly trained, very, very successful law enforcement agents. Their conviction rate usually hovers around 90%.

So the criminal division of the IRS is looking into you, you have a much higher rate of being convicted. You have a much higher rate of having some

negative consequence than you do on the civil side where the rate of penalties being upheld and paid is likely something less than that. When things go criminal, it tends to be more egregious cases. There are so-called badges of fraud that we look for. The more badges, the more egregious. And to be fair, they typically look a lot like the fact finding in the DeGuzman case, somebody buying a \$78,000 Mercedes on the eve of trial tends to look bad.

Warren Racusin: So is it in part a question that civil tax fraud is you did something bad, criminal tax fraud is you did something really, really, really bad? Is it that question of criminal intent? Is that part of the mix also?

Melissa Wiley: It is absolutely part of the mix. And maybe that on the criminal side it's more clear that you were trying to evade tax. You weren't just super, super sloppy or a little bit too aggressive, but you were really trying to evade tax.

Warren Racusin: It's what we learned in law school was called mens rea, the criminal intent.

Melissa Wiley: Those who have looked at when announcements of indictments in tax crimes get made, have noticed that they get made disproportionately in the first quarter of the year. And that is very specifically because they lock those things in people's minds right around tax filing season. So coming up on April 15th, you may notice more information about people who have not been forthright in their taxes in order to encourage everyone to file theirs correctly.

Warren Racusin: A little friendly persuasion from our friends at the IRS.

Melissa Wiley: Exactly.

Elie Honig: As a prosecutor, I mean this is a judgment call, this is an exercise of prosecutorial discretion. You'll get these cases, and you have to just consider all the real-world factors. There's no magical scientific formula that tells you, well, this one's criminal, this one's civil. You just have to look at the amount, the flagrancy of it. How extensive was the fraud? I mean look, this is being talked about now in the news in the Hunter Biden context. Hunter Biden was charged with felony tax evasion in California, in federal court in California. And there's a healthy debate which tends to break along, not coincidentally, probably the lines of what do you think of Hunter Biden or not? Or probably are you Democrat or Republican? I'm not going to weigh in on that.

But there's a healthy debate out there among former prosecutors and others of would this normally have been charged as a criminal misdemeanor or as a civil case, or is this appropriately being handled as a federal felony? And I think DOJ has tripped over itself here because they were originally willing to plead him out to a misdemeanor for probation, and then that deal fell apart in court because the parties didn't actually have a full meeting of the minds. And then DOJ turned around, they named special counsel, and now he's charged with a tax fraud felony.

Melissa Wiley: That's a great segue to you, Elie. When you were a prosecutor, you had a case that you mentioned at the top of the podcast. And we'd love to hear some more about that.

Elie Honig:

So like I said at the beginning, my disclaimer, I am not and have never been a tax lawyer. In fact, what I did primarily when I was with the US Attorney's Office in Manhattan was organized crime, mob cases. That said, it did creep up once in a while. And I actually had one case that went to trial where we had tax charges, but to set the scene, our case was against two members of the Gambino organized crime family. The lead defendant and the guy who we end up charging with tax crimes is a guy named Sal Scala. His mob nickname because they're always very descriptive and accurate, was Fat Sal. Guess why? Because he was fat. They're super creative. The co-defendant was a guy named Tommy Sassano who was sort of a bigger blustery guy. They were both capos, which is a high rank. It's like a mid-level supervisor within the mob. Both made guys.

Warren Racusin:

What a second. What was Tommy's nickname?

Elie Honig:

Tommy didn't really have one. I'm trying to think. Not everyone had one. Tommy may have had a lesser used one, but he was like, I'm trying to give a visual. Fat Sal was a heavyset guy. He looked like an ordinary gangster. Tommy Sassano was more like a big built like bull of a guy who they would use to intimidate people. And Fat Sal's claim to fame before this case was that if you all know mob history, probably the most famous modern hit that was ever done was when John Gotti Sr, essentially arranged a coup in 1985 where they murdered their own family boss Paul Castellano, out on the street of Manhattan outside of Spark Steakhouse, right? There are famous images of this, but Castellano, the boss was going in to have dinner at Spark Steakhouse, and John Gotti arranged for a bunch of guys to shoot and kill Castellano and the Underboss, a guy named Tommy Bilotti.

Well, one of the four shooters was always rumored and widely believed to be Fat Sal Scala. It was never proved. He was never charged with it, but it's sort of accepted mob cannon that Fat Sal was one of the shooters back in 1985 on this historic hit. Anyway, fast-forward to the late 2000s, the late 00s, and I land on this case where Fat Sal and Tommy Sassano were shaking down a strip club in Manhattan. Gosh, they called it 4040. So I think it keeps changing names like these strip clubs often do, but it's at the corner of 40th and fourth or something like that, or 40th Avenue or whatever, 40th Street, whatever it is. But it was one of the big sort of well-known strip clubs in Manhattan. And the crux of our case was the extortion charges. Count one and count two of the indictment were extortion and extortion conspiracy involving these two.

And then I don't remember exactly how we were not working with the IRS agents that Melissa mentioned earlier. This was straight up a case we did with the FBI, but they realized that Fat Sal had been making a lot of money from this extortion and others. I mean they were making six figures a year just from this extortion and paying no tax on it. And so the extremely nuanced, extremely difficult tax case that I got involved Sal Scala reporting and paying zero income and zero taxes for a stretch of about five years. But we still had to prove knowledge and willfulness and all the things you normally have to prove in a criminal case. And one of the great facts for us was that Scala actually did report taxes and pay taxes in a minuscule amount for the two years before the five years of 0000.

Elie Honig:

But the amounts he paid was like triple digits. It was like \$640 one year, making this up, and \$720. It was some ridiculously tiny amount, but at least it showed for our purposes as prosecutors. Well, he knows he has to pay taxes. He's done it in the past. And then he stopped. Now let me tell you what Fat Sal's defense was. Around the time he stopped paying taxes, the FBI had done a search warrant on Fat Sal's home and office, and as part of that search warrant, they seized a couple boxes, two boxes just of documents that he had sitting around his house. At our trial Fat Sal's lawyer said, "Well, the FBI had his financial documents, they had taken those boxes and so therefore he was unable to file his tax returns or pay any taxes." Now, there were a couple problems with this.

Number one is they never asked for them, they never raised this, they never said what was in it, but we had a little bit of a problem, which was we couldn't find those boxes. They had been seized by the FBI many years before. Things aren't always meticulously kept. And the judge was starting to come down on us basically saying, if you can't produce those boxes, you're going to have a problem. We got lucky. We sent an agent into some old archive basement facility, and he found the boxes. It was definitely them. They had been properly marked and linked to the search and everything. And so when we went through the boxes, it was absolute garbage. It was travel brochures, it was magazines, it was personal photos, nothing to do whatsoever with this guy's finances. And I will add one more wrinkle at trial, two more wrinkles if I can.

First of all, Scala called his own former lawyer. I can say the name because it's a matter of public record. He called his own former lawyer as a witness, a guy named Bruce Barket. And Bruce Barket said, "I told him, you're not to pay your taxes. You can't pay your taxes until you get those boxes back." Again, though the problem is nobody even asked the FBI, "Hey, can we get that back?" Nobody ever said to the IRS, "Hey, he can't pay until he gets his boxes back." The other problem was we were able to show that Barket knew full well this guy was a criminal and was paying him with criminal proceeds. So that was issue number one for Scala. Issue number two was the defense actually called an expert witness in this case, and he came up with some hooky calculation that yielded Scala owing a little bit of money, but only minimal money like a few hundred bucks each year.

But he made up these figures. Basically, Scala said, well, I'm a consultant. And so the expert said, well, a consultant on average would make \$80,000 a year, and he would have expenses for copier paper and he would have expenses for a printer. But I remember I cross-examined this expert. I said, "Where'd you get the \$80,000 a year figure?" He said, "Well, I assumed it." I said, "So you made it up?" He said, yeah. And I said, "Where are you getting the \$46 a year for copier paper? Are you saying that's how much Sal Scala actually spent?" He goes, "No, no, no. I assumed that that's what." I said again, "So you made it up." And I've had this go both ways. I'm not trying to be a hero here. I've definitely had moments where I felt juries pulling away from me, but as I was cross-examining, I could just feel the jury out of my peripheral vision like totally turning on this guy like who was this fraud of an expert.

It was the easiest tax case in human history, I think from a prosecutor's perspective. But we did end up convicting Scala and Sassano of the extortion and Scala of the tax case. I guess Tommy Sassano was paying his taxes or something. We didn't charge Sassano with any tax crime. So that is my one very amateurish, dabbling in the tax scenario. And so afterwards we joked like, hey, can we now say we're like financial prosecutors even though we only do this mob stuff? But that was my one little dalliance in the world of tax fraud. I'll take your questions.

Warren Racusin: Well, I still want to know Tommy's mob name. That's my big thing. But the great thing I have about our business, and Melissa sees it on the tax side, and we see it on the trust and estate side, is every time you think you've heard every possible story, the phone rings. You say what? And you're off to the races.

Elie Honig: Have you heard this one before? The FBI seized my documents in a search warrant years ago.

Warren Racusin: I was going to say that's a new one.

Melissa Wiley: I'm going to file my back pocket.

Warren Racusin: Yeah, really.

Melissa Wiley: When I have another argument.

Elie Honig: And let me tell you, when we got those boxes, they were old and dusty. They'd been at some storage facility. We were a little nervous. We were like, okay. I mean, if there are actually financial documents here, it still doesn't mean he's got a fully good defense, but there's something to it. I remember as we went through, we were just laughing. It was just the silliest crap. It was programs for the Yankees game. It was personal letters just from relative, from guys in prison had written him, other mobsters. It was actually useful but had nothing to do with, I don't think there was anything even resembling a financial document in there. So yeah, that was a good moment when we were sort of thumbing through those boxes.

Warren Racusin: Well, I think our takeaways from this entire discussion revolve around there's nothing wrong with legitimate tax avoidance. There is a difference between tax avoidance and tax evasion. And as one of my mentors always used to say, tax avoidance means you wear a suit with vertical stripes. Tax evasion means you wear a suit with horizontal stripes. If we haven't scared you straight already to make sure we have embellished the lessons of this episode in your brains, we close with a cautionary poem, style of Theodor Seuss Geisel. So then...

Elie Honig: Wait, can we just be clear before we read this? Who takes credit for the writing of this work of art? Is this you Warren or is this you, Melissa?

Warren Racusin: I am guilty as charged. Yes.

Elie Honig: Okay.

Warren Racusin: I wrote this while I was flat on my back recovering from getting an RSV and a COVID shot at the same time. And in my fever dreams, this came about.

Elie Honig: Well, it's a work of art and genius as we're about to say.

Warren Racusin: Oh my goodness, thank God, bless you. Ms. Wiley.

Melissa Wiley: All right. You tell me your income is meager and flat, but I see your lifestyle and I smell a rat.

Elie Honig: You purchase a Rolex for men and for ladies, and how could you pay for those brand-new Mercedes?

Warren Racusin: You may try to assert you're an innocent spouse, but that means you're calling your partner a louse.

Melissa Wiley: When the IRS sees this, they'll throw a huge fit. And you will not like jail, not one little bit.

Elie Honig: So take it from us three, you'd best not be naughty when it's time to sit down and fill out your 1040.

Warren Racusin: Or the revenue service will catch you for certain and visit upon you a world full of burden.

<music> *It was Christmas in prison and the food was real good. We had turkey and pistols carved out of wood. And I dream of her always, even when I don't dream her names on my tongue and her bloods in my strength.*

Warren Racusin: To the fabulous Melissa Wiley and Elie Honig and be sure to listen to Elie's podcast Up Against the Mob and Third Degree. They're terrific. Thanks to the crew with Lowenstein and Good to Be Social for helping us put these together. Thanks mostly to all of you for listening. Season three of Splitting Heirs coming up soon. We'll see you then. Until then, as we say in these parts, have a good one.

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