***Kwong v. Commissioner, 65 T. C. 959 (1976)***

A fraudulent spouse filing a joint tax return is liable for the entire fraud penalty on the deficiency, even if the income was community property and the other spouse was innocent of fraud.

**Summary**

In Kwong v. Commissioner, Joseph D. Kwong and his wife, Mee C. Kwong, filed joint federal income tax returns for 1967-1970. Joseph fraudulently underreported their community income, leading to a deficiency. The IRS asserted a 50% fraud penalty under section 6653(b) against Joseph for the full deficiency. The court held that despite Mee's innocence and the community nature of the income, Joseph was liable for the entire fraud penalty due to the joint and several liability inherent in joint returns. This decision clarifies that the 1971 amendment to section 6653(b) protects innocent spouses from fraud penalties but does not reduce the liability of the fraudulent spouse.

**Facts**

Joseph D. Kwong and Mee C. Kwong, residents of California, filed joint federal income tax returns for the taxable years 1967 through 1970. All income reported was community income under California law. Joseph was a wholesale flower grower and had fraudulently underreported their income, leading to deficiencies in tax. He pleaded guilty to tax evasion for 1969, and the charges for the other years were dismissed. Both spouses agreed to the deficiencies but disputed the fraud penalties. Joseph agreed to pay the fraud penalty on half of the deficiency but contested liability for the other half, citing the community nature of the income and Mee's innocence.

**Procedural History**

The IRS issued a notice of deficiency to both petitioners, determining that Joseph was liable for the full 50% fraud penalty under section 6653(b) for the deficiencies. The case was submitted to the United States Tax Court fully stipulated. The Tax Court ruled that Joseph was liable for the entire fraud penalty despite Mee's innocence and the community property nature of the income.

**Issue(s)**

1. Whether Joseph D. Kwong is liable for the entire amount of the 50% fraud penalty under section 6653(b) for the deficiencies in their joint income tax liability for the years 1967 through 1970, where the deficiencies resulted from the understatement of community income and were attributable to fraud solely on the part of Joseph.

**Holding**

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1. Yes, because the liability for the fraud penalty under section 6653(b) is joint and several, and the 1971 amendment to this section was intended to relieve only the innocent spouse of liability for the fraud penalty, not the fraudulent spouse.

**Court's Reasoning**

The Tax Court reasoned that under section 6013(d)(3), joint filers are jointly and severally liable for the tax, including penalties. The 1971 amendment to section 6653(b) was designed to relieve the innocent spouse of the fraud penalty, not to reduce the liability of the fraudulent spouse. The court cited previous cases like Nathaniel M. Stone and Parker v. United States, which supported the principle that the fraudulent spouse remains liable for the entire fraud penalty on the deficiency. The court rejected the argument that the community property nature of the income should affect the fraud penalty liability, emphasizing that the economic burden on the innocent spouse from community fund payments did not equate to legal liability. The court also noted that the legislative history did not suggest an intent to provide special treatment for community property states.

**Practical Implications**

This decision clarifies that in cases of joint tax returns where one spouse commits fraud, the fraudulent spouse is liable for the entire fraud penalty on the deficiency, regardless of the community nature of the income. This ruling guides attorneys in advising clients on the implications of filing joint returns and the potential liabilities for fraud penalties. It emphasizes the importance of understanding the scope of joint and several liability in tax law. The decision does not affect the protection given to innocent spouses under the 1971 amendment but reaffirms that such protection does not extend to the fraudulent spouse. Subsequent cases involving joint filers and fraud penalties should be analyzed in light of this ruling, which has been consistently applied in similar situations.

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