

Leonard – Unmarried Taxpayer Allowed Head of Household Status and Dependency Exemptions

The definition of what constitutes a "family" has undergone seismic change over the past two decades. For reasons of economic necessity, the traditional definition of family (one consisting of one or two parents and their children), has for many struggling at the margins of the economy morphed into something quite different. For some, family has become an arrangement where two individuals share goals and values, reside in the same dwelling place, and share living expenses.

As the definition of family changes, how the sharing of expenses, and how they are claimed on individual tax returns, is being felt in the tax system.

Marc Soss reviews a fascinating Tax Court case that deals with issues such as who is a dependent and who is permitted to claim child care and earned income credits.

EXECUTIVE SUMMARY:

In *Leonard v. Commissioner* (T.C. Summary Opinion 2008-141) a per se taxpayer was victorious on the issue of who is eligible to claim the dependency exemption. The end result was that an unmarried taxpayer, who was supporting her roommate and her roommate's two grandchildren, was entitled to claim "Head of Household" status on her federal income tax return and was also eligible to claim dependency exemptions under IRC Section 152.

FACTS:

BACKGROUND:

In 2005, Danita Leonard was unmarried and worked as a correctional officer at the Virginia Peninsula Regional Jail, She provided eighty (80%) percent of the 2005 household expenses for her roommate, her roommates grandchildren and herself. She was also enrolled in a college course in compliance with her job's requirements.

On her Federal income tax return for 2005, which was prepared by H&R Block, Danita claimed:

- 1) Head of Household status;
- 2) Adjusted gross income under \$30,000;
- 3) A dependency exemption deduction for each of her roommate's grandchildren;
- 4) A child care credit;
- 5) A child tax credit;
- 6) An earned income credit; and
- 7) An education credit.

IRS POSITION

The IRS responded to Danita's tax return with a notice of deficiency. The Service challenged her eligibility for:

- 1) Head of Household filing status;
- 2) Dependency exemption deductions;
- 3) A child care credit for one of the grandchildren;
- 4) Child tax credits for both grandchildren;
- 5) The earned income credit; and
- 6) Education credit for her college course work.

THE TAX COURT'S OPINION

Instead of paying the alleged deficiency, Danita represented *herself* all the way to the Tax Court, which ruled that Danita *was*:

- 1) Entitled to "Head of Household" status;
- 2) Eligible to claim a dependency exemption for her roommate
- 3) Entitled to claim dependency exemptions for the grandchildren because they each qualified as a "qualifying relative;"
- 4) Not entitled to a child tax credit for her roommate's grandchildren as they were not a "qualifying child;"
- 5) Not eligible for the earned income credit; and
- 6) Entitled to the education tax credit.

COMMENT:

Even though the decision in this case was entered under Section 7463(b), which means it cannot be treated as a precedent for any other case, the expanded definition of "qualifying relative" under IRC Section 152 could open the door to more taxpayers attempting to claim "Head of Household" filing status and dependency deductions.

The decision is interesting in part because the IRS argued against applying its own guidance from Notice 2008-5 which stated that an individual who is not treated as a qualifying child of another may qualify as a taxpayer's qualifying relative.

The repercussions of *Leonard* could also be felt in the guardianship and family law arenas, and it may only be a matter of time before creative planners attempt to apply its principles in the estate planning context.