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Analysis of the Head of Household Filing Status

By: Chau Le, *MST Student*

Tax Filing Status

When it comes to filing individual tax returns, one of the most important tasks for taxpayers is to figure out their filing status. Current tax law allows the following status: Single, Married Filing Jointly, Married Filing Separately, Qualifying Widow(er) with Dependent Child, and Head of Household.¹ As their names refer, only married taxpayers can elect to file as Married Filing Jointly or Married Filing Separately. A taxpayer is deemed married if his or her spouse dies during the taxable year.² Likewise, only unmarried taxpayers can elect to file as Single or Head of Household. Tax law defines a taxpayer as unmarried if the taxpayer is legally separated from his spouse under a decree of divorce or of separate maintenance, or if any time during the taxable year his spouse is not a non-resident alien.³ Besides, a married taxpayer who is not living with the spouse will be considered unmarried for the taxable year if he files a separate return and during the taxable year he maintains his house as a household of a child for more than one half of the year. The taxpayer must also provide more than one half of the cost of maintaining the house and does not live with his spouse during the last 6 months of the taxable year.⁴ For those that can file their tax returns as Head of Household, it allows them to claim a higher standard deduction putting them in lower tax brackets, as compared to the Single filing status, which eventually results in a favorable tax treatment for them. Specifically, for the tax year 2017, taxpayers filing as Head of Household can deduct \$9,350 from their taxable income as the basic standard deduction while those filing as Single can only deduct \$6,350 from their taxable income.⁵ Higher standard deductions normally result in lower taxable income, reducing the final amount of tax owed by taxpayers.

¹ IRC §1

² IRC §2(b)(2)(A), (B)

³ IRC §2(b)(2)(C)

⁴ IRC §7703

⁵ IRC §63

For the tax year 2017, federal tax rates for those filing as Head of Household and Single are shown in the following table:⁶

Heads of Household		Single	
If taxable income is	The tax is	If taxable income is	The tax is
Not over \$29,600	15% of taxable income	Not over \$22,100	15% of taxable income
Over \$29,600 but not over \$76,400	\$4,440 plus 28% of the excess over \$29,600	Over \$22,100 but not over \$53,500	\$3,315 plus 28% of the excess over \$22,100
Over \$76,400 but not over \$127,500	\$17,544 plus 31% of the excess over \$76,400	Over \$53,500 but not over \$115,000	\$12,107 plus 31% of the excess over \$53,500
Over \$127,500 but not over \$250,000	\$33,385 plus 36% of the excess over \$127,500	Over \$115,000 but not over \$250,000	\$31,172 plus 26% of the excess over \$115,000
Over \$250,000	\$77,485 plus 39.6% of the excess over \$250,000	Over \$250,000	\$79,772 plus 36% of the excess over \$250,000

According to the table, for the same amount of taxable income, Head of Household taxpayers will pay less tax than Single taxpayers do. For example, if taxable income is \$60,000, a Head of Household taxpayer will owe \$9,252.50 in tax while a Single taxpayer will owe \$10,738.75 in tax.

For tax saving purposes, more and more unmarried taxpayers prefer Head of Household status to Single status. However, among these taxpayers, many do not fully understand the requirements for electing the Head of Household status. The tax law imposes strict guidelines and taxpayers must satisfy certain requirements in order to file as a Head of Household.

⁶ IRC §1(b),1(c)

This article looks into the case of *Tommy J. Walker, Jr.*,⁷ where a taxpayer failed to satisfy the requirements for the Head of Household filing status, explores requirements for Head of Household status, and other items such as the dependency exemption, Child Tax Credits, the Additional Child Tax Credit, and the Earned Income Tax Credit. Additionally, we will also discuss the ruling of the judge in the case and provide an overview of the court proceedings.

Tommy J. Walker, Jr. v. Commissioner⁸

In this case, the taxpayer, Tommy J. Walker, Jr., lived with his girlfriend and her son during two full taxable years in an apartment. He paid a portion of the rent while the other portion was subsidized by the government. He also provided more than one half of financial support to his girlfriend's son.

During the taxable year, a daughter of the taxpayer's cousin moved into his apartment. However, the taxpayer could not provide sufficient evidence showing the amount of time she had lived with him.

For the two taxable years in dispute, Walker elected Head of Household status in his tax returns and claimed dependency exemption deductions for his girlfriend's son and his cousin's daughter. In addition, he took the Child Tax Credit, Additional Child Tax Credit, and the Earned Income Credit. The IRS disallowed the Head of Household status and also refused his claims for dependency exemption deductions as well as the before-mentioned credits. This resulted in deficiencies in Walker's tax returns.

Dependency Exemption Deductions

The tax code allows a taxpayer a deduction for every dependent the taxpayer has during the taxable year.⁹ IRC §152(a) defines a dependent as either a qualifying child or a qualifying relative:

An individual is a qualifying child of a taxpayer when he or she meets these requirements: (1) the individual is a child of the taxpayer or a child of the taxpayer's child, or the

⁷ TC Summary Opinion 2017-8

⁸ TC Summary Opinion 2017-8

⁹ IRC §151(c)

individual is a brother, sister, stepbrother, or stepsister of the taxpayer or a descendant of such relative, (2) the individual lives with the taxpayer for more than one half of the taxable year, (3) the individual is under 19 years old at the end of the taxable year (or if the individual is a full-time student that is under 24 years old at the end of the taxable year), (4) the individual does provide more than one half of his or her own support during the taxable year, and (5) the individual does not file a joint return with his or her spouse for the taxable year.¹⁰

Here, neither the girlfriend's son nor the cousin's daughter qualify as the taxpayer's qualifying child. Their relationships with the taxpayer were not included in those listed in §152. Therefore, Walker could not claim these children as his dependents under the qualifying child rules.

However, a taxpayer can also claim an individual as his dependent if the individual is a qualifying relative of the taxpayer. An individual is a qualifying relative if he or she meets the following requirements: (1) the individual is a child of the taxpayer or a descendant of such child; or the individual is the taxpayer's brother, sister, stepbrother, stepsister, father, stepfather, mother, stepmother, brother's son or daughter, sister's son or daughter, father's brother or sister, mother's brother or sister, son-in-law, daughter-in-law, father-in-law, mother-in-law, brother-in-law, or sister-in-law; or the individual, other than taxpayer's spouse, lives with the taxpayer for the whole taxable year¹¹, (2) the individual's gross income is less than the exemption amount of \$4,050¹², (3) more than one half of the individual's support during the taxable year is provided by the taxpayer, and (4) the individual is not a qualifying child of the taxpayer or of any other taxpayer during the taxable year.¹³

In Walker's case, he claimed dependency exemption deductions for his girlfriend's son and his cousin's daughter, believing that they were his qualifying relatives. However, for his cousin's daughter, the taxpayer could not either establish the amount of time she lived in his household or proved that he provided more than one half of the support to her. The

¹⁰ IRC §152(c)

¹¹ IRC §152(d)(2)(H)

¹² Internal Revenue Service, Publication 501, Exemptions, Standard Deduction, and Filing Information for use in preparing 2017 Returns. Retrieved from <https://www.irs.gov/pub/irs-pdf/p501.pdf>

¹³ IRC §152(d)

judge agreed with the commissioner and denied Walker's dependency exemption deductions with respect to the cousin's daughter.

For the girlfriend's son, Walker managed to provide sufficient evidence showing that the child lived with him during the whole taxable years in dispute and that he provided the child more than one half of the child's support.¹⁴ Therefore, he could claim the girlfriend's child as his dependent. The judge granted Walker dependency exemption deductions for the child as a qualifying relative.

Child Tax Credit and Additional Child Tax Credit

Besides the dependency exemption deductions, Walker also claimed the Child Tax Credit and Additional Child Tax Credit. These credits are provided for in IRC §24. These credits, for the years at issue, generally allowed a credit of \$1,000 against his or her taxable income for every qualifying child he or she has.¹⁵ An individual qualifies as a qualifying child of a taxpayer needs to meet all the requirements as previously mentioned under the dependency exemption rules.¹⁶

As it was determined that Walker had no qualifying child with respect to his girlfriend's son and his cousin's daughter, he was not entitled to this Child Credit. The judge rules in favor of the IRS and denied Walker the Child Tax Credits and Additional Child Tax Credits.

Earned Income Tax Credit

The tax code allows certain taxpayers a credit against their taxable income if his or her earned income does not exceed a specific amount that is known as earned income amount. This credit is ruled under IRC §32 and known as the Earned Income Credit. A taxpayer is eligible for the Earned Income Tax Credit if he or she has a qualifying child or, in the case the taxpayer does not have a qualifying child, the taxpayer must live in the United State more than one half of the taxable year, is at least 25 years old in the taxable year, and is not

¹⁴ This satisfies §152(d)(2)(H)

¹⁵ IRC §24(a) and (c)(1)

¹⁶ IRC §152(c)

a dependent of any other taxpayers.¹⁷ The earned income amount is generally determined based on the number of qualifying children and the filing status of the taxpayer.¹⁸

Walker's earned income was determined to exceed the applicable earned income amount and therefore, disqualified him for the Earned Income Credit. Accordingly, the judge disallowed him to claim earned income tax credit.

Head of Household Filing Status

Another dispute, in this case, concerned the tax filing status of Head of Household. As discussed earlier, Head of Household status puts an unmarried individual in an advantageous tax bracket (as compared to those filing as Single), generally resulting in lower tax liability. Section 2 of the Internal Revenue Code provides the conditions that a taxpayer has to meet if he or she wants to elect the head of household status. Specifically, the taxpayer must be (1) not married at the close of the taxable year, and (2) maintain his home as a household of a qualifying child, a dependent, or the mother or father of the taxpayer. A dependent is either a qualifying child or a qualifying relative as defined in §152 of the Code.¹⁹

Walker was not married during the taxable year and he maintained the household he lived in during the taxable year. Therefore, he could elect Head of Household status if he also had a dependent that lived with him during the taxable year. Although it was determined that Walker had no qualifying child during the taxable year, his girlfriend's son met the conditions to be his qualifying relative.

Section 152(d)(1) provides that an individual is a taxpayer's dependent if (1) he or she has a relationship with the taxpayer as defined in section 152(d)(2), (2) has gross income less than the personal exemption amount, (3) receives more than one-half of the support provided by the taxpayer, and (4) is not a qualifying child of other taxpayers.

Available evidence in the case showed that Walker provided more than one-half of the support of his girlfriend's son and the child was not a qualifying child of any taxpayer. The child had no other source of income. The child's relationship with Walker is included in the

¹⁷ IRC §32(c)(1)(A)(ii)

¹⁸ IRC §32(b)(2)(A)-(B)

¹⁹ See Dependency Exemption Deductions.

definition of §152(d)(2)(H) because he lived with Walker during the taxable year. Therefore, the child was dependent on Walker. Based on the foregoing, it can be concluded that Walker met all the conditions to file his tax return as a Head of Household.

Therefore, on this particular matter, the Tax Court disagreed with the IRS and allowed Walker to elect Head of Household status on his tax returns. However, it appears that there is a flaw in the judge's decision over the Head of Household status of the taxpayer, which is to be discussed in the following section.

The Tax Code Needs to be Read in its Full Context

Section 2 of the Internal Revenue Code provides the conditions for a taxpayer to claim the Head of Household filing status. At the same time, this section also sets some limitations that prevent a taxpayer from filing as Head of Household even though he may preliminarily meet all the requirements imposed by the code.

Section 2(b)(3) states that a taxpayer is not a Head of Household during the taxable year if he or she is a non-resident alien in any time of the year, or if the taxpayer has a dependent under §152(d)(2)(H). In other words, if an individual is qualified as a dependent of a taxpayer under section 152(d)(2)(H), and the taxpayer only has this individual as his dependent, the taxpayer is not eligible for Head of Household status.

Section 2(b)(3) also sets forth another limitation for the Head of Household status regarding the support requirement. Accordingly, a taxpayer is deemed to provide over one half of the support to his dependent during a taxable year if no other person contributes over one half of the support, the taxpayer contributes over ten percent of the support, and other individuals who contribute more than ten percent of the support agree to write a declaration that they will not claim the dependent on their tax returns.²⁰ Section 2(b)(3) states that if a taxpayer provides more than one half of the support to his dependent only because of the above-mentioned conditions, he is not entitled to the Head of Household status.

Coming back to the facts of the case, since Walker established that he provided over one half of the support to his girlfriend's child, the second limitation is not applied in this case.

²⁰ IRC §152(d)(3)

We will discuss the application of the first limitation. As discussed above, the child of Walker's girlfriend qualified as his dependent under §152(d)(2)(H), however, because of the first limitation set forth in §2(b)(3), Walker would not be eligible for the Head of Household status.

If the judge had taken into account of the limitations under section 2(b)(3), he would have agreed with the commissioner and denied Walker his Head of Household status. This article does not look into the reasons why the judge missed the limitations; however, it is more than likely that the judge would have changed his ruling if he had noticed the limitations. This is to emphasize the importance of reading a tax code in full context before interpreting the code. Due to tax law's complexities and its ever-changing nature, limitations and specials rules are very common in the tax code and could be unnoticed if a code reader does not exercise thorough reading.

In this case, the judge's ruling regarding Head of Household status cannot be reversed because the taxpayer chose small case procedure when he filed his petition. Small case procedure prevents the IRS from appealing the case although the IRS is more than likely to win the case if it is appealed.

Tax Court: Taxpayer Responsibilities and General Procedures

In general, in a petition with the U.S. Tax Court, a taxpayer has the burden of proof when the IRS determines deficiencies in the taxpayer's return.²¹ That is, the taxpayer is responsible for proving that the determination of the Commissioner is wrong or erroneous.

In the case of any deficiencies, a taxpayer has two options: (1) pay the deficiency or (2) file a petition with the Tax Court. Generally, a taxpayer will choose to file a petition to the Tax Court because it does not require the taxpayer to pay the deficiencies before a ruling is determined. If the taxpayer chooses to file a petition with a U.S. District Court, or U.S. Court of Federal Claim he or she will have to write a check for the determined deficiencies before the petition can be filed.

The Tax Court also allows a petitioner to potentially file small case claim, which was used by Walker. In order to file a small case claim with the Tax Court, the disputed amount

²¹ Tax Court Rule 142(a)

(including interest and penalties) must not exceed \$50,000. Small cases provide for a simpler and faster trial with fewer formalities than regular case petitions. However, once a ruling is given for a small case, neither party can appeal the decision.

This can help explain why the IRS Commissioner did not appeal the case and Walker was allowed to file as Head of Household, although the judge appeared to overlook the limitations of section 2(b)(3) and made a wrong decision over the matter.

Recap

Tax deductions and tax credits are a matter of legislative grace. That means a taxpayer cannot claim any deductions or credits unless they are lawfully allowed by the tax code. As a corollary, a proper interpretation of the tax code is imperative for a taxpayer to determine his or her eligibility for any tax deductions or credits. Likewise, a taxpayer has to comply with the tax code when he determines his tax filing status.

In Walker's case, he failed to substantiate his claims for dependency exemptions, Child Tax Credits, and Additional Child Tax Credits and Earned Income Tax Credits. Also, as discussed, although the Tax Court allowed Walker to file as Head of Household, he should have been denied this status. As a result, this failure of substantiation resulted in additional taxes for Walker.

Underpayment of tax may also lead to penalties and interests. Interests start to accrue from the due date for tax payment and will continue to accrue to the date the taxpayer pays the tax deficiencies. If a taxpayer decides to bring his case to the Tax Court before paying the deficiencies and does not prevail in the end, he will accumulate more interests. In order to fully comply with the tax code, a taxpayer should maintain a good record of documents relevant to their tax standing. If a taxpayer does not fully understand their tax position, it is recommended that the taxpayer seek advice from a professional and experienced practitioner.