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Exemptions for Dependents: The Burden of Proof Dilemma for Divorced or Separated Parents

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RECENT DEVELOPMENTS

EXEMPTIONS FOR DEPENDENTS: THE BURDEN OF PROOF DILEMMA FOR DIVORCED OR SEPARATED PARENTS

Plaintiff, divorced and living apart from his former wife who had custody of their two sons, claimed dependency exemptions[1] for both sons in his federal income tax returns for the two years in question. The Commissioner of Internal Revenue disallowed the exemption for one son in each of the two years. In affirming the Commissioner's determination, the Tax Court held that plaintiff failed to sustain the burden of proving that his contribution was more than half the total support of the children.[2] Though able to establish the amount of his contribution, plaintiff could not prove the amount of support from all other sources, including his former wife. On appeal to the Fourth Circuit, reversed. *Held:* To sustain the burden of proof for a claimed dependency exemption, a taxpayer need not prove the total amount of support from all sources if he establishes other facts persuasively indicating that his contribution constituted over half the claimed dependent's aggregate support. *Commissioner v. Mendel,* 351 F.2d 580 (4th Cir. 1965).[3]

Section 151(e), Internal Revenue Code of 1954, allows a taxpayer an exemption of $600 apiece for those of his children who receive over fifty per cent of their total support from him during the calendar year. Under Tax Court rules of practice[4] a taxpayer has the burden of

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[1] INT. REV. CODE of 1954, § 151(e)(1), provides:
An exemption of $600 for each dependent (as defined in section 152)—
INT. REV. CODE of 1954, § 152(a) states:
[T]he term "dependent" means any of the following individuals over half of whose support ... was received from the taxpayer ... (1) A son or daughter of the taxpayer....

[2] Walter H. Mendel, 41 T.C. 32 (1956).

[3] 24 J. TAXATION 50 (1966).

[4] Rule 32 of Rules of Practice of the Tax Court, 26 CFR § 701.32 provides: The burden of proof shall be upon the petitioner, except as otherwise provided by statute, and except that in respect of any new matter pleaded in his answer, it shall be upon the respondent.
The Code imposes the burden of proof upon the Commissioner on issues of transferee liability, § 6902(a); and intent to evade tax in civil fraud actions, § 7454(a).
Rule 32 applies only to Tax Court cases, although it has been applied in district court cases to assessments made by the Commissioner. 9 MERTENS, LAW OF FEDERAL INCOME TAXATION § 50.61 n.98 (1943).

proving his right to a claimed exemption[5] by a preponderance of the evidence.[6] The Tax Court has repeatedly held that it cannot make the percentage computation contemplated by the statute unless it knows the total amount of child support from all sources, as well as the amount contributed by the taxpayer.[7] The principal case represents a departure from this rule in the case of a divorced husband who is prevented from claiming exemptions, to which he might otherwise be entitled, because of inability to prove the support contribution of his estranged wife with whom the dependents live.[8]

The court in the principal case noted that proof of the total amount of support received by the claimed dependents was a crucial fact in most cases,[9] but that the Code itself did not expressly require such proof.[10] Although plaintiff was unable to establish the amount of his former wife's contribution, the court held that he had met the contribution requirement by showing that his sons were young, modestly dressed, had no extraordinary medical or education expenses, and together received annually from him approximately one thousand five hundred dollars support. Without explanation, the court stated that

[5] In addition to Rule 32, a taxpayer faces the obstacle that deductions are a matter of legislative grace, and qualification is dependent upon strict compliance with the Code. 2 CASEY, FEDERAL TAX PRACTICE § 7.9 (1955).

A taxpayer also faces a presumption that the Commissioner's determination is prima facie correct. Unless this determination is palpably erroneous, arbitrary, or capricious, a petitioner must produce competent evidence to rebut the presumption, regardless of the difficulty in producing such evidence. The burden of proof remains on the petitioner even after he has introduced sufficient evidence to overcome the presumption. Balter, *Rules of Evidence Applicable in Proceedings before the Tax Court of the United States: Burden of Proof and Presumptions*, 6 MARQUETTE UNIVERSITY INSTITUTE ON TAXATION 1 (1956).

[6] 9 MERTENS, *op. cit. supra* note 4, § 50.62.

[7] Zacker, ¶ 53,275 P-H Tax Ct. Mem., at 834 (1953):

> The petitioner did not offer evidence as to what the total support of the children was, and it is not possible for us to make a finding ... [that the husband's payments] constituted half the support....

Accord, Weidler, ¶ 55,130 P-H Tax Ct. Mem. (1955); Kessler, ¶ 55,203 P-H Tax Ct. Mem. (1955) (husband's unsupported opinion of actual total support insufficient); McDevitt, ¶ 54,068 P-H Tax Ct. Mem. (1954) (evidence of support costs in prior years insufficient); Banzhaf, ¶ 53,294 P-H Tax Ct. Mem. (1953) (unsupported testimony concerning wife's income and support contribution, and state court support order insufficient).

[8] See Clurman, *Exemptions for Dependents*, 21 J. TAXATION 306 (1964); Lagomarcino, *The Divorced Husband and the Dependency Exemption Mirage*, 12 TAX L. REV. 85 (1957).

[9] The court cited Kennedy v. Commissioner, 339 F.2d 335 (7th Cir. 1964); Fearing v. Commissioner, 315 F.2d 495 (8th Cir. 1963); Tressler v. Commissioner, 206 F.2d 538 (4th Cir. 1953).

[10] *But see*, Treas. Reg. § 1.152-1(a)(2)(i) (1957), as amended, T.D. 6441, 1960-1 CUM. BULL. 51, which provides:

> For purposes of determining whether or not an individual received ... over half of his support from the taxpayer, there shall be taken into account the amount of support received from the taxpayers as compared to the entire amount of support which the individual received from all sources....

the principal case was like two Tax Court cases, *Theodore Milgroom*[11] and *E. R. Cobb, Sr.*,[12] in which exemption was allowed without proof of a divorced wife's support contribution. The court also stated without criticism that *Bernard C. Rivers*,[13] on which the Tax Court in the principal case relied, was distinguishable. While allowing the exemption without a showing of total amount of support, the court also approved of other circuit court decisions[14] which followed the general rule requiring proof of the total amount, without giving an explanation for the exception to this rule made in the principal case.

By recognizing the possibility of a taxpayer proving his right to dependency exemptions without necessarily showing total support, the principal case provides some measure of relief for taxpayers facing the persisting burden of proof dilemma. The court's failure, however, to give any explanation in its decision other than a recitation of facts, leaves uncertain the full scope of this exception to the usual proof requirement. The decision implies that this exception will benefit few taxpayers since cases before the Tax Court seldom correspond with the factual situation in *Mendel*.

In those cases following the general rule, proof of total support was needed because, unlike *Mendel*, one or more of the following circumstances were present: plaintiff established no other evidence than the amount of his contribution;[15] the evidence was unpersuasive, without a showing of total support, that a contribution met the required amount;[16] there was contradictory evidence in the record; substantial support payments of an unascertained amount from other

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[11] 31 T.C. 1256 (1959).

[12] 28 T.C. 595 (1957). In neither *Milgroom* nor *Cobb* did the divorced husband prove total support for his children. As in the principal case, however, the husband presented sufficient facts to persuade the Tax Court that he had contributed more than one half his children's support. *Cobb* recognized the husband's burden of proof dilemma, but neither decision mentioned that it was deviating from the general rule requiring proof of total support. *Milgroom* and *Cobb* were not cited by the Tax Court in the principal case.

[13] 33 T.C. 935 (1960). In Cohan v. Commissioner, 39 F.2d 540 (2d Cir. 1930), the court held that once a taxpayer's *right* to a deduction was established the *amount* of the deduction could be determined by approximation. The court in *Rivers*, a dependency exemption case, refused to apply the *Cohan* principle of approximation to determine a taxpayer's right to an exemption by approximating the dependent's total support. Since the right to the dependency exemption was contingent upon the total amount of support, *Cohan* could not apply. This holding is inapplicable when, as in *Mendel*, proof of total support is unnecessary to establish an exemption right.

[14] See note 9 *supra*.

[15] Kennedy v. Commissioner, 339 F.2d 335 (7th Cir. 1964); Tressler v. Commissioner, 206 F.2d 538 (4th Cir. 1953); Kessler, ¶ 55,203 P-H Tax Ct. Mem. (1955).

[16] Fearing v. Commissioner, 315 F.2d 495 (8th Cir. 1963); Weidler, ¶ 55,130 P-H Tax Ct. Mem. (1955).

sources were shown; and plaintiff's contribution had to be allocated between dependents and nondependents.[17]

Several other approaches exist to that normally taken in determining whether the taxpayer's contribution meets the fifty percent support test. The court in the principal case could have compared the taxpayer's contribution with various governmental statistics indicating average costs of support for the number of dependents claimed.[18] If the taxpayer's contribution equalled or exceeded one half of the average support cost, a presumption could arise that the support test had been met, the burden of introducing rebuttal evidence then shifting to the Commissioner.[19]

A second approach exists when the total amount of support appears to consist only of contributions by the parents. Since the contribution of one of the parents constitutes over half the total support, as a practical matter one of them is entitled to the exemption. If only the husband claims the exemption and proves the amount of his contribution, as in *Mendel,* allowing his exemption would be reasonable regardless of whether or not he proved the amount of total support. The alternative to this approach is to give the exemption to the wife or no one.[20] This would allow a wife not entitled to an exemption either to claim it herself, or prevent her husband from taking it, by remaining silent.

A third possible approach exists if both parents claim the exemption and only the husband has kept accurate records. Assuming again that only the parents have contributed to the dependent's support, the husband should be allowed the exemption without regard to proof

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[17] Fearing v. Commissioner, *supra* note 16; Rivers, 33 T.C. 935 (1960).

[18] See generally U.S. DEP'T. OF COMMERCE, STATISTICAL ABSTRACT OF THE UNITED STATES 363-65 (86th ed. 1965):

Table 498 - *Comparative Cost-of-Living Indexes, by Family Size and Income Before Tax, 20 Cities: 1963...*

Table 499 - *Annual Budget Costs—City Workers' Families and Retired Couples, 20 Cities: 1959.*

Table 500 - *Indexes of Annual Budget Costs—City Workers' Families and Retired Couples, 20 Cities: 1959.*

See also *Comparison of individual Income tax exemptions with estimated budget amounts at the maintenance level for families of different sizes (September, 1949),* TAX ADVISORY STAFF, U.S. TREASURY DEP'T, as cited and revised in SURREY & WARREN, FEDERAL INCOME TAXATION 412-13 (1960 ed. 1962).

[19] In *Mendel* plaintiff contributed $1,625 in 1957 and $1,529 in 1958 as support for both children. According to Table 499, STATISTICAL ABSTRACT, *supra* note 18, this amount exceeded one-half the average total annual budget costs of a city worker's family of four.

[20] This alternative would counter the legislative purposes in granting and subsequently increasing the exemption amount to relieve some minimum standard of living from direct taxation, offset rising costs of living, and stimulate the economy. S. REP. No. 1013, 80th Cong., 2d Sess. (1948).

of total support.[21] The alternative is again either denying an exemption altogether, or giving it to the wife; thus penalizing her former husband for keeping records and allowing her to claim forgetfulness whenever her records in fact supported his claim.

Aside from these possibilities, the court failed to discuss whether the traditional burden of proof rule is properly applicable in dependency exemption cases involving divorced or separated parents. The usual reason given for presuming that the Commissioner's determination is correct[22] is the taxpayer's access to the evidence.[23] When divorced or separated parents claim a dependency exemption, this reason for the presumption is often invalid. Living apart from his former spouse, the taxpayer lacks knowledge of her actual expenses. Likewise, testimony of dependents is generally incompetent or unreliable.[24] When a wife claims the support exemption for her children, section 7213 of the Code prohibits the Internal Revenue Service from giving the divorced husband information on the amount and items contributed by his wife.[25] The wife frequently refuses to appear as a voluntary witness; and the husband has little recourse if she ignores a subpoena.[26] Even if she does appear, her testimony usually is of

[21] *Cf.* Starkey, ¶ 63,272 P-H Tax Ct. Mem. (1963) (exemption claimed by both spouses granted to one maintaining records). Another approach was adopted in Lai, ¶ 62,087 P-H Tax Ct. Mem. (1962), when both parents claimed the exemption, supported only by estimates. The court suggested that each parent claim an exemption for one of the two children. Upon the wife's refusal to compromise, both exemptions were granted to the husband.

[22] See note 5 *supra.*

[23] Carrano v. Commissioner, 70 F.2d 319, 321 (2d Cir. 1934). In O'Laughlin v. Helvering, 81 F.2d 269, 270 (D.C. Cir. 1935), the court stated:

> When a deduction is claimed, the government has an undoubted right to demand a full disclosure of the facts on which the claim is based, for otherwise it would be at the mercy of the unscrupulous taxpayer . . . as the government should never be overreaching or tyrannical, neither should a taxpayer be permitted to escape payment by the concealment of material facts.

See 9 MERTENS, *op. cit. supra* note 4, § 50.61; Balter, *supra* note 5, at 20.

[24] Lagomarcino, *supra* note 8.

[25] INT. REV. CODE OF 1954, § 7213(a)(1) provides in part:

> It shall be unlawful for any officer or employee of the United States to divulge or to make known in any manner whatever not provided by law to any person the ... [information] ..., or any particular thereof, set forth or disclosed in any income return....

The Internal Revenue Service has ruled that the husband requesting information contained in his former wife's return may be informed only that the amount reported by him is insufficient to establish his right to the claimed dependency exemption. Rev. Rul. 58-120, 1958-1 CUM. BULL. 498. For the effect of a Tax Court subpoena requiring the Commissioner to produce such information, see text accompanying notes 31-34 *infra.*

[26] INT. REV. CODE OF 1954, § 7456(a) provides:

> [A]ny judge of the Tax Court may... require, by subpoena ordered by the Tax Court... (1) the attendance and testimony of witnesses, and the production of all necessary returns, books, papers, documents, correspondence, and other evidence....

The Tax Court, however, lacks authority to punish for non-compliance. Enforcement requires separate action in a district court. The small amount ordinarily

little value.[27] Moreover, the wife is often antagonistic or vindictive because of personal hostility towards the husband and possible loss of the exemption herself. Her lack of knowledge or failure to remember can effectively prevent the husband from establishing the total cost of support necessary to satisfy his burden of proof.[28] Under such circumstances, a presumption favoring the Commissioner's determination seems unreasonable and inequitable.[29]

Another injustice of the strict burden of proof rule in divorced-parent dependency exemption cases is that revenue agents customarily appear only in support of the Commissioner's case. An unresolved issue is whether the Tax Court may effectively require the Commissioner to produce tax returns of third parties or other relevant records, when a taxpayer himself lacks access to necessary facts.[30] The Tax Court's authority to subpoena witnesses and records has been upheld[31] as a limitation upon the statute[32] prohibiting disclosure by Treasury officials of information in their possession. Nevertheless, attempts by taxpayers before the Tax Court to subpoena revenue agents as witnesses against the Commissioner usually are unsuccessful. Internal revenue officers are instructed not to produce official

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at stake before the Tax Court effectively precludes this as any real threat. Lagomarcino, *supra* note 8.

[27] See, *e.g.*, Banzhaf, ¶ 53,294 P-H Tax Ct. Mem. (1953).

[28] Dyer, ¶ 55,168 P-H Tax Ct. Mem. (1955). In Sijan, ¶ 55,287 P-H Tax Ct. Mem. (1955), the court noted:

> Petitioner is in the unfortunate position of having to rely upon the testimony of his divorced wife for proof of the total amount expended in maintaining the children, who lived with her. Even granting the correctness of petitioner's assertion that this witness's testimony may have been exaggerated and unreliable, there is no escape from the conclusion that if we disregard it the record is barren of any evidence in this vital area. Petitioner is merely left with an unproved case.

[29] This presumption has been characterized by Judge Learned Hand as a "rubric which has saved the Treasury many a doubtful case, but which can easily be pushed to deny taxpayers privileges plainly theirs." Taylor v. Commissioner, 70 F.2d 619, 620 (2d Cir. 1934), *aff'd*, 293 U.S. 507 (1935).

Nevertheless, the presumption has been applied in numerous tax cases not involving exemptions, when proof was impossible. 9 MERTENS, *op. cit. supra* note 4, § 50.62. Lack of proof preventing the taxpayer from overcoming the presumption may also prevent him from sustaining the burden of proof, even in the presumption's absence.

In Balter, *supra* note 5, at 25-26, it is stated that this presumption is stronger that the usual presumption which disappears whenever contrary evidence is introduced, and it actually constitutes evidence for purposes of determining whether the burden of proof has been met.

[30] 2 CASEY, *op. cit. supra* note 5, § 7.43.

[31] Blair v. Oesterlein Co., 275 U.S. 220 (1927), in which the court observed:

> The prohibition is limited to disclosures made ... [in any manner whatever not provided by law]. It cannot be deemed to forbid disclosures made in obedience to process lawfully issued in a judicial or quasi-judicial proceeding....

See 2 CASEY, *op. cit. supra* note 5, § 7.43.

[32] See note 25 *supra*.

records or testify in response to any subpoena without the Commissioner's express authorization.[33] Moreover, cases and writers disagree on whether failure to comply with a subpoena shifts the burden of proof to the Commissioner or has any other tangible adverse effects.[34] Consequently, attacking the presumptively correct determination of the Commissioner as being based upon unreliable evidence, often proves futile unless the taxpayer himself has knowledge of all the necessary facts.

Even if this presumption was not applied in dependency exemption cases, a taxpayer would still face the difficult burden of proving his right to the exemption.[35] Difficulty in obtaining necessary facts does not shift the burden of proof to the Commissioner;[36] and the benefit of the *Mendel* exception to normal proof requirements will extend to few taxpayers. Because of the uncertainty in this recurring question, inequitable results will continue so long as the Tax Court must decide exemption cases solely upon failure of one party to sustain the burden of proof. It is submitted that the taxpayer's problem of establishing facts necessary for a dependency exemption will not

[33] Mim. 6727, 1952-1 CUM. BULL. 234, 236 quotes from article 80 of Regulations 12, as amended by T.D. 5428, 1945 CUM. BULL. 462, and T.D. 4640, 1936-1 CUM. BULL. 495:

> revenue officers are ... prohibited ... to produce ... records or copies thereof ... whether in answer to subpoena duces tecum or otherwise, or to testify to facts coming to their knowledge in their official capacities without express authority from the Commissioner....

As support for this policy, Mim. 6727 cites Boske v. Comingore, 177 U.S. 459 (1900). In *Boske* the federal employee involved was called only as a witness and the government was not a party to the action. Kentucky-Tennessee Light & Power Co. v. Nashville Coal Co., 55 F. Supp. 65 (W. D. Ky. 1943), distinguished *Boske* as inapplicable where the Commissioner was a party. Plaintiff in *Nashville Coal* was seeking only information concerning parties to the action. The case therefore avoids the problems of a husband seeking information in returns of his former wife who is not a party to the dependency exemption case.

[34] That the Commissioner's non-compliance with a Tax Court subpoena does *not* shift the burden of proof to the Commissioner, see Darling Bros. Co., 2 B. T. A. 612 (1925), and 9 MERTENS, *op. cit. supra* note 4, § 50.61. *Contra*, Wodehouse, 8 T. C. 637 (1947), *aff'd*, 337 U.S. 369 (1949), *reversing*, 166 F.2d 986 (4th Cir. 1948). In *Wodehouse* the subpoenaed records concerned only the petitioner's returns, and the court did not consider the effect of the Commissioner's refusal to produce records of a third person.

That the Commissioner's failure to produce subpoenaed evidence raises an inference that such evidence is unfavorable to him, see 2 CASEY, *op. cit. supra* note 5, § 7.44.

[35] See note 5 *supra*.

[36] See cases cited note 29 *supra*. In Burnet v. Houston, 283 U.S. 223, 228 (1931) (dictum), the Court said:

> the impossibility of establishing a specific fact, made essential by the statute... [does not justify] a decision for the taxpayer based upon a consideration only of the remaining factors which the statute contemplates....The impossibility ...simply leaves the claimant upon whom the burden rests with an unenforceable claim ... as a result of a failure of proof.

Since the taxpayer is initiating the Tax Court's proceedings, placing the burden of proof on him is no more unjust than placing it on a plaintiff in any civil

be resolved in continual litigation. Some more practical solution should be sought through legislation supported by the Treasury Department.[37]

PURCHASE OF NOTE CONSTITUTES USURIOUS LOAN

Defendant applied for a loan to an investment broker to whom he gave a mortgage and a promissory note payable to, and subsequently endorsed in blank by, a third party. The broker, whose name appeared on neither instrument, then sold the 6,000 dollar note at a six per cent discount to plaintiff after deducting a commission of 890 dollars. Defendant received only 4,750 dollars for his note. Plaintiff did not know that his money constituted the original consideration for the note, which bore ten per cent annual interest. After defendant's default, plaintiff brought this action to foreclose the mortgage. The trial court concluded that the transaction was in substance a usurious loan and sustained the defense of usury. On appeal, the Washington Supreme Court affirmed in a five-four decision. *Held:* The defense of usury is available to the maker of a note for which no value has previously been given if it is discounted at a rate which, when added to stated interest, exceeds the statutory maximum, even though plaintiff holder did not know that he furnished the original consideration. *Baske v. Russell,* 67 Wash. Dec. 2d 264, 407 P.2d 434 (1965).

The Washington usury statute, limited in application to loans and forbearances,[1] does not affect the sale and purchase of negotiable

litigation. Balter, *supra* note 5, at 20. The strict burden of proof rule has also been defended on the ground that the Tax Court itself is not equipped to investigate and present factual evidence. Morrisdale Coal Mining Co., 19 T.C. 208 (1952); Producers Crop Improvement Ass'n, 7 T.C. 562 (1946). See 9 MERTENS, *op. cit. supra* note 4, § 50.62; Balter, *supra* note 5.

[37] See articles cited note 8 *supra,* for possible legislative and administrative solutions to the taxpayer's burden of proof problem in dependency cases. See also Kaminsky, *The Case for Discovery Procedure in the Tax Court,* 36 TAXES 498 (1958). The problems illustrated by the principal case often could be avoided by providing in the alimony decree at the time of divorce that child support be incorporated within alimony payments. The wife would get the dependency exemption, but the husband would be able to deduct the entire alimony payment. See Commissioner v. Lester, 366 U.S. 299 (1961).

[1] WASH. REV. CODE § 19.52.020 (1957):

> Any rate of interest not exceeding twelve percent per annum agreed to in writing by the parties to the contract, shall be legal, and no person shall directly or indirectly take or receive in money, goods or thing in action, or in any other way, any