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MEMORANDUM FOR ASSISTANT DISTRICT COUNSEL,
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FROM: George J. Blaine, Chief, Branch 1
Office of Income Tax and Accounting CC:DOM:IT&A

SUBJECT: Significant Service Center Advice
Foster Child and Revenue Ruling 77-280

This memorandum responds to your request for advice dated September 24, 1999, forwarding questions from the Centralized Quality Review Site (CQRS). CQRS asked for clarification of Rev. Rul. 77-280, 1970-2 C.B. 14, and ILM 1999034, concerning when a foster parent may claim a dependency deduction for a foster child under sections 151 and 152 of the Internal Revenue Code (the Code) and when a foster parent may claim a charitable deduction for unreimbursed foster care expenditures under section 170 of the Code.

ISSUES

1. Whether a foster parent may allocate unreimbursed foster care expenditures so as to take both a dependency deduction for a foster child under sections 151 and 152 of the Code and a charitable deduction under section 170 of the Code.
2. Whether a foster parent may choose between the dependency deduction and the charitable deduction.
3. If a foster parent may not choose between the dependency deduction and the charitable deduction, how could a foster parent meet the support test under section 152(a)?

CONCLUSIONS

The character of unreimbursed foster care expenditures will depend of the facts of a particular situation.

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1. A foster parent may not allocate unreimbursed foster care expenditures so as to take both a dependency deduction and a charitable deduction.
2. A foster parent may not choose between a dependency deduction and a charitable deduction.
3. In some situations, the unreimbursed foster care expenditures will not qualify for the charitable deduction. These foster care expenditures may qualify as support under section 152(a), and a foster parent may claim a foster child as a dependent if the requirements of sections 151 and 152 are met.

DISCUSSION

Section 151(a) of the Code allows a deduction for the exemptions provided by that section. Section 151(c)(1)(B) allows an exemption for a dependent of the taxpayer who is a child of the taxpayer and who, at the close of the calendar year, is under age 19 or a student under age 24. Section 151(c)(3) defines the term "child" to include a son or daughter of the taxpayer. Section 152(b)(2) states that a foster child is treated as a natural child of the taxpayer if the requirements of section 152(a)(9) are met. Section 152(a)(9) provides that, for the entire tax year, the foster child's principal place of abode must be the taxpayer's home and the foster child must be a member of the taxpayer's household. Under the general rule of section 152(a) of the Code, the taxpayer must provide over half of the foster child's support for the calendar year in which the tax year of the taxpayer begins.

Section 170(a) of the Code allows a deduction for a charitable contribution. Section 170(c) defines a charitable contribution as a contribution or gift to or for the use of a governmental agency described in section 170(c)(1) or a charitable organization described in section 170(c)(2).

Section 1.170A-1(g) of the Income Tax Regulations allows a charitable deduction for unreimbursed expenditures made incident to the rendition of services to an organization, contributions to which are deductible under section 170 of the Code.

CQRS asked for clarification of the conclusions of Rev. Rul. 77-280, 1977-2 C.B. 14, concerning Situations 1 and 2. Those situations describe fact patterns in which the foster parents do not have a profit objective but are reimbursed, in whole or in part, for their expenditures in providing foster care. The foster parents do not receive payments from a charitable organization in excess of their foster care expenses. Regarding these situations, the ruling states that "[t]he foster parents are entitled to a charitable contribution deduction within the limitations of section 170 of the Code for any unreimbursed out-of-pocket expenses incurred in supporting a foster child." The ruling concludes that the foster parents in these

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situations can not claim a deduction under sections 151 and 152 of the Code for expenditures treated as a charitable contribution under section 170 of the Code. These conclusions of the ruling are limited to situations in which the unreimbursed expenditures of the foster parent meet the requirements for a charitable deduction under section 170 of the Code.

The case law supports the conclusion that the character of the unreimbursed expenditures of a foster parent is determined by the facts of a particular situation. A foster parent's unreimbursed out-of-pocket expenditures may benefit the foster child as well as the charitable organization responsible for the care of the child. See Tate v. Commissioner, 59 T.C. 543, 550 (1973) (stating that expenses incurred in the rendition of services to a qualified charitable organization may, and often do, benefit both the charity and the taxpayer). Whether these expenditures qualify for a charitable deduction will depend on whether the expenditures are made primarily to benefit the charitable organization. See Thomason v. Commissioner, 2 T.C. 441 (1943); McMillan v. Commissioner, 31 T.C. 1143 (1959). In Thomason, the taxpayer paid for the support and private education of a designated ward of the Illinois Children's Home and Aid Society. The court found that the taxpayer intended to benefit an individual boy in whom he had a keen fatherly interest and for whom the payments secured special privileges and advantages which the society otherwise would not have furnished. The court concluded that the payments the taxpayer made for the boy's support and education at a private institution were not made to or for the use of the society, even though the payments relieved the society of some financial burden. Similarly, in McMillan, the taxpayers supported a child whom the Family and Children's Association, a recognized charitable organization, was legally obligated to support until her final adoption. The court denied a charitable contribution to the taxpayers for this support because the court thought that the taxpayers provided the support to further their primary objective of adopting the child, even though that support relieved the Association of an obligation it would otherwise have been forced to meet. The court stated that "whatever charitable motives might have been present lose all color when viewed in the light of the inherently personal aspects of the situation." Id. at 1147.

Section 170(g) is instructive on the issue. Section 170(g) allows a charitable deduction for limited amounts paid by the taxpayer to maintain certain students as members of the taxpayer's household. This provision does not allow a charitable deduction, however, when the student is the taxpayer's dependent, as defined in section 152.

Finally, CQRS asked for clarification of ILM 1999034. ILM 1999034 addressed the narrow question of why the I.R.S. deleted certain language from Publication 17. That language categorically stated that a foster parent may not take a dependency exemption for a foster child if the foster parent receives any payments for foster care from a state, a political subdivision of a state, or a tax-

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exempt placement agency. ILM 1999034 explained that the IRS deleted the language from the publication because a foster parent may meet the support test under section 152(a) of the Code, despite receiving some foster care payments from a governmental agency or a tax-exempt agency.

The ILM states that foster care payments from a governmental agency or tax-exempt agency count toward the foster child's total support, but not as support provided by the foster parent, in determining whether a foster parent provided over one-half of the child's support under section 152(a). The ILM addressed only the support calculation under section 152(a) of the Code. ILM 1999034 should not be read to allow a foster parent to claim both a dependency deduction and a charitable deduction for unreimbursed expenditures or to allow a foster parent to choose between a dependency deduction or a charitable deduction.

If you have any questions concerning this advice, please call Victoria Driscoll at (202) 622-4910.