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Consider tax deductions for relatives this tax season

Are you are baby boomer caught in the "sandwich generation?" Are you supporting parents as well as adult children? CNBC.com recently shared an article by Jackson Hewitt Tax Service, Inc., reported by the Associated Press on January 25, 2013, suggesting that deductions for dependents are more available than you might think. The defining question is who is a dependent? Now is the time to determine if you might have dependents that you just did not realize could be counted as such by the IRS.

The economy has resulted in a changing family dynamic according to Bob Meighan, vice president of Turbo Tax, an online tax preparation service. Anyone who is caught between aging parents who lost a good part of their retirement savings in the Great Recession and are now running out of assets, and adult children who cannot find employment and therefore are returning (or never leaving) home will agree wholeheartedly with Mr. Meighan. People are living longer, which puts a strain on retirement savings. Many adult children are supporting elderly parents, perhaps even paying for expensive care. An example from the IRS gives some guidance. "Your mother received $2,400 in Social Security benefits and $300 in interest. She paid $2,000 for lodging and $400 for recreation. If you spend more than $2,400 to support her, supplementing what she spends, and if her annual income is less than $3,800, you can claim her as a dependent and take the full value of the exemption."

Taxpayers may be aware of the ability to claim an elderly parent or parent as a dependent; what is less well known is that you may be supporting other relatives that may qualify as dependents. Mark Steber, chief tax officer at Jackson-Hewitt Tax Services remarked that "rules are very pro-taxpayer." If you are taking care of someone and that person's care meets the IRS guidelines for age, income, residency tests and support, you might be able to claim the exemption. A qualifying relative does not need to live with you, but you must provide at least one half of his or her support. Furthermore, that person's income cannot exceed the personal exemption of $3,800 in 2012. A qualifying relative can be a child who does not meet the qualifying child guidelines, a parent or stepparent, grandparent, niece or nephew, aunt or uncle or in-laws. Usual support items are the cost of housing, food, clothing, and medical costs. Steber suggests thinking beyond the nuclear family situation.

Jackie Perlman, principal tax research analyst for H&R Block, points out the tax filer's vision should not just be focused on the personal exemption. There is an "extra benefit" for filing as head of household if that filer can legally claim children, parents or other relatives as a dependent. For example, the 15 percent tax bracket applies to taxable income up to $47,350 for heads of households, but $35,350 for individual returns. At the 25 percent tax bracket, it is $133,300 for heads of households as opposed to $85,650 for single filers.

The bottom line is that filers should pay attention to the dependency issue when filing their federal income tax forms. You might find relief in an unexpected quarter. It is also a good time to look ahead to next year to see if careful records and a small increase in support of a relative can "buy" you an exemption next year.