De Mars v. Commissioner, 79 T. C. 247 (1982)

Married couples must aggregate their income to determine eligibility for the disability income exclusion under IRC section 105(d).

Summary

In De Mars v. Commissioner, the U. S. Tax Court upheld the IRS's denial of a disability income exclusion claimed by Owen and Corinne DeMars on their 1977 joint return. The court ruled that under IRC section 105(d)(3), the DeMars' combined adjusted gross income exceeded the statutory threshold, thus phasing out their eligibility for the exclusion. Additionally, the court dismissed the DeMars' constitutional challenge to the income aggregation requirement for married couples, finding it rationally justified and not discriminatory.

Facts

Owen DeMars retired on disability in 1971 and was permanently and totally disabled. In 1977, the DeMars filed a joint tax return claiming a $5,200 disability income exclusion. Their combined adjusted gross income for that year, excluding the claimed disability income, was $22,471. 25. The IRS disallowed the exclusion based on the phaseout provisions of IRC section 105(d)(3), which reduce the exclusion when adjusted gross income exceeds $15,000.

Procedural History

The IRS issued a notice of deficiency to the DeMars in 1980, disallowing the disability income exclusion. The DeMars petitioned the U. S. Tax Court, which heard the case and issued its decision on August 10, 1982, affirming the IRS's position and entering a decision for the respondent.

Issue(s)

1. Whether the DeMars were entitled to a disability income exclusion under IRC section 105(d) for 1977.
2. Whether the requirement under IRC section 105(d)(5)(B)(ii) that married persons must aggregate their income for purposes of the disability income exclusion is unconstitutional.

Holding

1. No, because their combined adjusted gross income exceeded the statutory threshold of $15,000 by more than the amount of the exclusion claimed, thus phasing out their eligibility under IRC section 105(d)(3).
2. No, because the requirement to aggregate income for married couples is rationally justified and does not unconstitutionally discriminate against them.

Court’s Reasoning

The court applied the statutory provisions of IRC section 105(d), specifically the phaseout rule in section 105(d)(3), which reduces the disability income exclusion when adjusted gross income exceeds $15,000. The court noted that the DeMars’ combined income exceeded this threshold by $7,471. 25, thus eliminating their eligibility for any exclusion. Regarding the constitutional challenge, the court found that the DeMars did not properly raise the issue in their pleadings. Even if properly raised, the court held that the requirement to aggregate income for married couples under section 105(d)(5)(B)(ii) had a rational basis, as explained in the Senate Report, aiming to direct tax benefits more fairly to low- and middle-income taxpayers. The court emphasized that tax exclusions are matters of legislative grace and upheld the aggregation requirement as not violating due process or equal protection under the Constitution.

Practical Implications

This decision clarifies that for married couples seeking the disability income exclusion, their combined income must be considered, potentially affecting their eligibility. Tax practitioners must advise clients on the importance of considering total household income when planning to claim such exclusions. The ruling reinforces the principle that tax benefits are subject to legislative discretion and that income aggregation rules for married couples are constitutional. Subsequent cases may reference De Mars when addressing similar issues of income aggregation for tax benefits, and it underscores the need for precise statutory interpretation in tax law.

