

***Carolyn Pratt Perry v. Commissioner of Internal Revenue, 92 T. C. 470 (1989)***

Unpaid alimony does not establish a basis for a bad debt deduction, and not all child care expenses qualify for a child care credit.

**Summary**

Carolyn Perry sought tax deductions and credits for unpaid alimony and child care expenses after her ex-husband failed to make court-ordered payments. The Tax Court ruled that Perry had no basis in the alimony debt for a bad debt deduction under section 166, as her expenditures were independent of her ex-husband's obligations. Additionally, Perry was denied a child care credit for her children's airfare to visit grandparents but was allowed a credit for paying the employee's share of a babysitter's social security taxes. This case clarifies the criteria for bad debt deductions and child care credits, emphasizing the necessity of a basis in the debt and the specific qualifications for what constitutes an employment-related expense.

**Facts**

Carolyn Perry and Richard Perry divorced in 1975, with Richard ordered to pay \$400 monthly for child support and up to \$400 in alimony depending on his income. Richard failed to make these payments in 1980, 1981, and 1982. During these years, Carolyn spent more on child support than she received from Richard. She also paid for her children's airfare to visit their grandparents during school holidays and covered the employee's share of social security taxes for a babysitter. Carolyn claimed bad debt deductions for the unpaid alimony and child care credits for the airfare and social security taxes.

**Procedural History**

Carolyn Perry filed petitions with the U. S. Tax Court challenging the IRS's denial of her claimed deductions and credits for the tax years 1980, 1981, and 1982. The IRS had determined deficiencies and additions to tax, which Carolyn contested. The cases were consolidated for trial, briefs, and opinion.

**Issue(s)**

1. Whether Carolyn Perry was entitled to bad debt deductions under section 166 for arrearages in alimony payments from her ex-husband.
2. Whether Carolyn Perry was entitled to a child care credit for transportation expenses paid for her children.
3. Whether Carolyn Perry was entitled to a child care credit for paying the employee's share of social security taxes on behalf of a babysitter.

**Holding**

1. No, because Carolyn had no basis in the debt; the alimony payments were independent of her expenditures.
2. No, because the airfare expenses did not qualify as employment-related expenses under section 44A.
3. Yes, because paying the employee's share of social security taxes constituted part of the babysitter's compensation, qualifying as an employment-related expense.

### **Court's Reasoning**

The court applied section 166, which requires a basis in the debt for a bad debt deduction. Carolyn's expenditures were independent of Richard's alimony obligations, thus she had no basis in the debt. The court followed *Swenson v. Commissioner*, where similar circumstances resulted in the denial of a bad debt deduction. Regarding the child care credit, the court relied on section 44A and its regulations, determining that airfare did not qualify as care under section 44A(c)(2)(ii) because it was transportation to the care provider, not care itself. However, paying the babysitter's social security taxes was considered part of her compensation, qualifying under section 44A as an employment-related expense. The court also noted that post-hoc guarantees, like the one Carolyn attempted to use to establish a basis in the debt, were ineffective.

### **Practical Implications**

This decision clarifies that for a bad debt deduction, a taxpayer must have a basis in the debt, which is not established by independent expenditures. It also specifies that child care credits are limited to expenses directly related to care, not transportation to care. Practically, this means taxpayers seeking bad debt deductions for unpaid alimony must demonstrate a direct link between their expenditures and the debt. For child care credits, attorneys should advise clients that only expenses that directly constitute care will qualify. This ruling impacts how similar cases are analyzed and emphasizes the importance of understanding the specific qualifications under sections 166 and 44A. Subsequent cases, such as *Zwiener v. Commissioner*, have further explored these principles, particularly regarding the tax treatment of payments made on behalf of employees.