***Leah M. Carlebach and Uriel Fried v. Commissioner of Internal Revenue, 139 T. C. 1 (2012)***

In Carlebach v. Comm'r, the U. S. Tax Court upheld the validity of a regulation requiring children to be U. S. citizens during the tax year to be claimed as dependents. The court rejected the taxpayers' argument that the children's citizenship at the time of filing should suffice, affirming the annual accounting principle in tax law. This ruling impacts taxpayers with children who become citizens after the tax year in question, limiting their ability to claim dependency exemptions and related credits retroactively.

**Parties**

Leah M. Carlebach and Uriel Fried were the petitioners in this case. They were married and filed joint returns for the years 2004, 2005, and 2006. Leah M. Carlebach also filed individual returns for the years 2007 and 2008. The respondent was the Commissioner of Internal Revenue.

**Facts**

Leah M. Carlebach and Uriel Fried, who resided in Israel, had six children, all born in Israel. The children were granted certificates of citizenship in 2007 and 2008. The Carlebachs filed their tax returns for 2004, 2005, and 2006 in December 2007, claiming dependency exemptions and various credits for their children. Leah M. Carlebach filed her 2007 and 2008 returns in October 2008 and June 2009, respectively, also claiming exemptions and credits for the children. The Commissioner disallowed these claims, asserting that the children did not meet the citizenship requirement during the relevant tax years.

**Procedural History**

The Commissioner issued notices of deficiency for the years 2004-2008, disallowing the dependency exemptions and related credits, and imposing penalties and additions to tax. The Carlebachs petitioned the U. S. Tax Court to challenge these determinations. The court considered the validity of the regulation requiring citizenship during the tax year for dependency exemptions, the eligibility for child care credits, and the appropriateness of the penalties and additions to tax. The court's decision was to be entered under Rule 155 of the Tax Court Rules of Practice and Procedure.

**Issue(s)**

Whether the regulation requiring a dependent child to be a U. S. citizen at some time during the tax year to qualify for a dependency exemption deduction is valid?

Whether Leah M. Carlebach was eligible for a child care credit for 2008 without filing a joint return?

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Whether the accuracy-related penalties and additions to tax for late filing were properly imposed?

**Rule(s) of Law**

Section 151(c) of the Internal Revenue Code allows a taxpayer a deduction for each dependent as defined in section 152. Section 152(b)(3)(A) stipulates that a dependent does not include an individual who is not a U. S. citizen or national unless a resident of the U. S. or a contiguous country. Section 1. 152-2(a)(1) of the Income Tax Regulations further specifies that to qualify as a dependent, an individual must be a citizen or resident of the United States at some time during the calendar year in which the taxable year of the taxpayer begins. Section 21(e)(2) requires married taxpayers to file a joint return to be eligible for the child care credit.

**Holding**

The court held that section 1. 152-2(a)(1) of the Income Tax Regulations is valid, and thus, the Carlebachs could not claim their children as dependents for the tax years before the children obtained their certificates of citizenship. Leah M. Carlebach was not eligible for a child care credit for 2008 because she did not file a joint return. The court sustained the accuracy-related penalties and additions to tax for late filing.

**Reasoning**

The court applied the Chevron two-step analysis to determine the validity of the regulation. First, it assessed whether Congress had directly spoken to the precise question at issue. The court found that the statute did not unambiguously address the timing of the citizenship requirement, but the context of the annual accounting system in the Internal Revenue Code suggested that the regulation was consistent with statutory intent. In the second step, the court found that the regulation was a reasonable interpretation of the statute, given the longstanding nature of the temporal requirement since 1944. The court also rejected the Carlebachs' argument that the children possessed derivative citizenship during the relevant tax years, emphasizing that citizenship was conferred only upon the receipt of certificates in 2007 and 2008. The court further reasoned that Leah M. Carlebach's failure to file a joint return disqualified her from the child care credit for 2008, and the penalties and additions to tax were appropriate due to the Carlebachs' negligence and lack of reasonable cause for their claims.

**Disposition**

The court affirmed the Commissioner's determinations, sustaining the disallowance of dependency exemptions and related credits, the denial of the child care credit for 2008, and the imposition of accuracy-related penalties and additions to tax for late filing. The decision was to be entered under Rule 155.

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**Significance/Impact**

Carlebach v. Comm’r reinforces the importance of the annual accounting principle in tax law, particularly in the context of dependency exemptions. The decision clarifies that the citizenship requirement must be met within the tax year, impacting taxpayers who may have children naturalized after the relevant tax year. It also underscores the necessity of filing a joint return to claim the child care credit, affecting married taxpayers filing separately. The case serves as a reminder of the strict application of tax regulations and the potential consequences of non-compliance, including penalties and additions to tax.

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