How Taxes Relate to California Divorce: Dependency Exemptions

There are four basic ways taxes have an impact on your California divorce: support, filing status, property division, and dependency exemptions. Here's a brief overview on what you need to know about how allocating dependency exemptions affect you in your divorce.

During the marriage, you probably didn't think twice about claiming your children as dependents on your joint tax returns. Parents are automatically entitled to a dependency exemption for each child they support. A dependency exemption is basically a tax deduction: the exemption reduces your taxable income so you ultimately pay less income tax and therefore have more net income.

Although the value to you is ultimately dependent on your income, the IRS adjusts the maximum amount the exemption is worth each year. So for example, in 2013, the exemption was worth $3,900. In 2014, the value was increased to $3,950, and in 2015, the amount was $4,000.

How Dependency Exemptions are Divided When Parents Divorce

The first rule is that a single exemption cannot be divided. In other words, if you only have one dependency exemption, only you or your spouse gets to claim it. There is no such thing as a half of a dependency exemption.

If the two of you cannot agree on who claims the dependency exemptions, the IRS automatically gives the exemptions to the custodial parent. The custodial parent is defined as the person who has the children more than half of the time in his or her home.

If, however, you do agree that the non-custodial parent should take the dependency exemptions, the custodial parent should sign IRS Form 8332. This form officially releases the exemptions to the non-custodial parent and creates clarity on both parents' individual tax returns.

How Dependency Exemptions Affect Child Support

So if the dependency exemption results in tax savings, why would anyone voluntarily give it up? The answer is because there is a relationship between who claims the children on taxes and the amount of child support.

Child support is based in large part on how much net income each parent has. When a parent utilizes a dependency exemption, his or her net income is increased. If the payor of child support has more net income, that person has more income available to pay child support, which in turn benefits the child support payee. Likewise, if the payee of child support has more net income, that person has more income, which reduces the payee's need for child support and thereby reduces the payor's child support obligation.

In many situations, making a smart financial decision on who claims the children as dependents will allow both parents to maximize their tax savings and net income. Take for example a stay at home parent. Since that person's income is less than the value of the dependency exemption, he or she derives no financial benefit from claiming a child on taxes. Meanwhile, the payor of child support could use all the boosting of net income he or she can get. In that case, it makes perfect sense for the payor to claim the children and the payee to in turn receive a higher amount of child support.

For help on deciding whether you or the other parent should claim the children as dependents for tax purposes, contact us for more information.