

# Tax Effects of Divorce, Marital Separation and Support Agreement

Lester I. Bowman

---

## Repository Citation

Lester I. Bowman, *Tax Effects of Divorce, Marital Separation and Support Agreement*, 2 Wm. & Mary L. Rev. 297 (1960), <http://scholarship.law.wm.edu/wmlr/vol2/iss2/2>

TAX EFFECTS OF DIVORCE,  
MARITAL SEPARATION AND SUPPORT  
AGREEMENTS\*

LESTER I. BOWMAN\*\*

In reviewing the cases involved in the subject of my discussion, I was reminded of a three-ring circus. In the center ring I found the Commissioner of Internal Revenue, and in the rings on either side the husband and wife. It was interesting to note, also, that when the wife was the petitioner, the Internal Revenue Service took the position that the monies received by her from her husband represented taxable income to her. Oddly, when the husband was the petitioner, the position was frequently taken that his payments to his wife were not taxable income to her and, therefore, not deductible by him.

Of course, I cannot resolve all of the problems involved in divorce, marital separation and support agreements during the time allotted to me. I can safely state, however, that domestic difficulties can be very costly, especially to the husband, so if you have any thoughts about the week-end I suggest that you approach your problem with extreme personal caution.

In this discussion, I shall use the word "alimony" to refer generally to all types of payments, including support or maintenance prior to divorce, which are deductible by the husband and includable in the wife's income.

---

\*Lecture delivered at the Tidewater Tax Conference.

\*\*Member, Virginia State Bar, Virginia State Bar Association, and American Bar Association, former member of Committee on Taxation of the Virginia Bar Association and of the Committee on Bureau practice and procedure and Committee of Statutes of Limitation, Tax Section, American Bar Association; former attorney, Chief Counsel's Office, Internal Revenue Service. Author, "Family Partnerships under Old and New Tax Laws." Lecturer at Tax Conferences of the University of Virginia. LL.B., University of Virginia.

The Tax Court has rejected the claim that taxing the wife on "alimony" is unconstitutional. *Twinam v. Comm.*, 22 TC 83. Further, the fact that payments are not viewed as "alimony" under the state law is of no moment.<sup>1</sup> For example, the support payments made to a wife after her remarriage are deductible by her former husband in determining his net taxable income, and are taxable to her even though there is no support obligation under the state law.<sup>2</sup>

Periodic alimony payments are deductible by the husband under the following conditions:

- (1) Pursuant to written separation agreements executed after August 16, 1954.
- (2) Pursuant to a decree or court order for support or maintenance entered after March 1, 1954.
- (3) Pursuant to a decree of divorce or separate maintenance or pursuant to written instruments incident to divorce or separation.

The first two categories became a part of the law as a result of the Revenue Act of 1954, while the third has been carried over from the 1939 Internal Revenue Code.

#### I. PERIODIC PAYMENTS UNDER WRITTEN SEPARATION AGREEMENTS EXECUTED AFTER AUGUST 16, 1954. [SECTION 71(a)(2) 1954 IRC]

Periodic payments are deductible by the husband and taxable to the wife if made under a written agreement executed after August 16, 1954, but provided the said payments are received by the wife after that date. This is so in spite of the fact that there is no court decree of divorce or separation and even though the decree is not legally enforceable. It is important to note, however, that H and W must be separated and living apart. If they are later legally divorced or separated, payments under the agreement are deductible and do not be-

---

1. *Brown v. U. S.* 121 F. Supp. 106, 46 AFTR 53.

<sup>2</sup> *Estate of Frances B. Willson*, TC Memo 1957-89.

come subject to the stricter rules applicable to deductibility under agreements incident to a divorce or legal separation.<sup>3</sup>

If a joint return is filed by the husband and wife, all is nullified, and H gets no deduction and W is not deemed to have received income.<sup>4</sup>

Separation agreements executed prior to August 17, 1954, but *materially* altered after August 16, 1954 are deemed to be executed after August 16, 1954 as to payments made by H and received by W after that date. Even though the agreement is not altered materially after August 16, 1954, payments made under an earlier agreement can still give rise to a deduction on the grounds that it is an agreement incident to a divorce or legal separation.

It is interesting to note that the wife must include alimony in her gross income, even though it is paid by the husband out of income which is tax exempt to him.<sup>5</sup> The husband can also deduct payments made to his wife, even if the wife is exempt from tax because she is a citizen of Puerto Rico.<sup>6</sup>

## II. SUPPORT PAYMENTS UNDER DECREE OR COURT ORDER ENTERED AFTER MARCH 1, 1954.

Support payments made under a decree or court order entered after March 1, 1954 are deductible by the husband only if they are received by the wife after August 16, 1954 and a joint return is not filed for the taxable year. It is not necessary that there be a divorce or legal separation under court order or a written separation agreement. The mere decree for support will suffice to justify the deduction.<sup>7</sup>

---

<sup>3</sup> Reg. 1.71-1(b)(2).

<sup>4</sup> Sec. 71(a)(2), Reg. 1.71-1(b)(2) and 1.71-1(c)(1)(ii).

<sup>5</sup> Neeman, 26 TC 864.

<sup>6</sup> Rev. Rul. 56-585, CB 1956-2, 166.

<sup>7</sup> Sec. 71(a)(3) 1954 IRC, Reg. 1.71-1(b)(3).

Temporary alimony ordered by the court pending the outcome of an action for divorce or separation can qualify for deduction by the husband if the decree is entered after March 1, 1954.<sup>8</sup> The Treasury has ruled that temporary alimony, ordered by the court pending a wife's action to set aside her husband's Mexican divorce and to grant her a legal separation, paid by the husband was deductible by him in determining his net taxable income. Thus, prior divorce does not disqualify payments made under a court order entered after March 1, 1954.<sup>9</sup> Further, a decree entered prior to March 1, 1954, but altered or modified by court order subsequent to that date is treated as a decree entered after March 1, 1954.<sup>10</sup> If a prior decree is not modified after March 1, 1954, the payments made by virtue of the decree are not deductible.<sup>11</sup>

Both the Treasury and Courts have ruled that an interlocutory decree does not affect a divorce or legal separation, therefore, payments made under such decrees entered before March 2, 1954 are not deductible. It is important to remember that alimony payments cannot be made deductible by means of a retroactive divorce or separation decree. Thus, a decree *nunc pro tunc* is of no effect. The Tax Court so held in *Daine v. Comm.*, 9 TC 47 affd. 168 F(2d) 449.

The above rules on deductibility and/or taxability of payments under a court decree for support entered after March 1, 1954 became effective with the Revenue Act of 1954. They apply generally to the taxable years beginning after December 31, 1954 and ending after August 16, 1954. Regulations make it clear that they also apply to the taxable years beginning before January 1, 1954 and ending after August 16, 1954, although such years are subject to the 1939 IRC.<sup>12</sup>

---

<sup>8</sup> Reg. 1.71(b)(3) and (6).

<sup>9</sup> Rev. Rul. 57-113, CB 1957-1, 106.

<sup>10</sup> Reg. 1.71-1(b)(3)(ii).

<sup>11</sup> Clayton TCM 1957, 183.

<sup>12</sup> Reg. 1.71-2.

### III. PAYMENTS MADE UNDER DECREE OF DIVORCE OR SEPARATE MAINTENANCE OR UNDER AGREEMENT INCIDENT TO THE SAME.

In order for payments to qualify as alimony under this category, the payments must meet the following conditions:

- (1) The parties must be divorced or legally separated under a decree of divorce or separate maintenance.
- (2) Payments must be periodic, though not necessarily made at regular intervals.
- (3) Payments must be received after the decree is granted.
- (4) The legal obligation discharged must be one imposed upon the husband because of a marital or family relationship.
- (5) The obligation must be made specific by the decree or by a written instrument incident to the divorce or separation.<sup>13</sup>

Before proceeding further, you are reminded that Congress imposes the tax and determines the deductibility and no divorce decree can change this.<sup>14</sup> Where there is uncertainty as to whether alimony payments are deductible by the husband and taxable to the wife, the parties should see that the decree provides for an adjustment in alimony in the event that such payments are determined to be non-deductible by the husband. The husband, in most cases, will agree to more substantial alimony if he can secure for himself a deduction for tax purposes. This should be borne in mind by counsel for both parties.

As stated, the parties must be divorced or legally separated under a decree of divorce or separate maintenance in order for the payments to be deductible as alimony. The Tax Court in *Fuqua v. Comm.*, 27 TC 909 held that the husband and wife were legally separated if the decree of separate maintenance recognized and sanctioned the separation, even though the decree

---

<sup>13</sup> Sec. 71(a)(1) 1954 IRC.

<sup>14</sup> Casey 12 TC 224.

failed to provide that they were entitled to live apart. This is not true of a mere court order for support which does not pass upon the legality of the separation. Payments made under such an order for support are not deductible unless the court order was entered after March 1, 1954.

A Mexican divorce obtained in good faith will support an alimony deduction, even though it is not recognized by the state wherein the wife resides.<sup>15</sup> A divorce, legal where granted, is sufficient to justify a deduction for alimony as far as the husband is concerned.<sup>16</sup> Payments made before the decree under a separate agreement later incorporated in the decree are not deductible.<sup>17</sup> However, payments made before the decree of divorce or separate maintenance may be deductible if they qualify under a written separation agreement executed after August 16, 1954, or pursuant to a decree or court order entered after March 1, 1954. Similarly, payments of temporary alimony may be deductible if they qualify as payments under a court order or decree for support entered after March 1, 1954, but alimony payments cannot be made deductible by means of a retroactive divorce or separation decree.

To be deductible, alimony payments must also be periodic, but this does not mean that they have to be paid at regular intervals. For example, the Treasury has ruled that payments for an indefinite period awarded under an interlocutory decree are periodic, even though at least a year must lapse between the interlocutory and final decree.<sup>18</sup> However, when payments are limited to the duration of the interlocutory decree (12 months for example), they are *not* deductible because they are considered installment payments rather than periodic payments.<sup>19</sup>

To qualify as "periodic", the payments need not be made at regular intervals. However, they must meet certain tests which are set forth as follows:

---

<sup>15</sup> GCM 25250, CB 1947-2, 32.

<sup>16</sup> *Feinberg v. Comm.*, 198 F(2d) 260 (3CCA-1952).

<sup>17</sup> *Fox* 14 TC 1131; *Black* TCM 3/12/51.

<sup>18</sup> IT 3761, CB 1945, 76.

<sup>19</sup> IT 3934, CB 1949-1, 54; IT 3944, CB 1949-1, 56.

- (a) If the total amount to be paid is not specified or readily ascertainable from the decree or written instrument incident thereto, the payments are "periodic". For example, payments of so many dollars per month until the death or remarriage of the wife.
- (b) If the total amount is stated or readily ascertainable from the decree or written instrument incident thereto, the payments to qualify as "periodic" must be made at intervals extending over a period of more than ten years. For example, \$12,100.00 payable at \$100.00 per month would qualify as periodic since the payments would extend over a period of ten years and one month from the date of the decree or written instrument incident thereto. An installment payment on the principal sum is considered "periodic" only to the extent that the installment payment or the sum of the installment payments received during the wife's taxable year does not exceed 10% of the principal sum. This 10% limitation applies to the installment payments made in advance, but does not apply to delinquent installments for a prior taxable year of the wife made during her current taxable year.<sup>19-1</sup>
- (c) If the total amount to be paid is stated in (or readily ascertainable from) the decree or written instrument incident thereto and the payments are to be made over a period of ten years or less from the date of the decree or written instrument incident thereto, the payments may or may not be "periodic". It depends on whether or not the payments are to be discontinued or altered by the death or change in economic status of the husband or wife or by the wife's remarriage.<sup>20</sup> For example, under the terms of a written agreement H is required to make payments to W., which are in the nature of alimony, in the amount of \$100.00 per month for nine years. These payments would not qualify as "periodic", but if the instrument further provided that if H or W dies the payments are to cease, then the payments would be considered "periodic".<sup>21</sup>

<sup>19-1</sup> Sec. 71(c)(2), Regs. 1.71-1(d)(2).

<sup>20</sup> Sec. 71(c) 1954 IRC, Regs. 1.71-1(d)(3)(i); Young, 10 TC 724.

<sup>21</sup> Regs. 1.71(d)(5) Example 1.



A husband who is committed to make periodic payments may reach an agreement with his wife whereby he discharges his obligation by giving her a lump sum instead of continuing with his periodic payments. No part of the lump sum, thus paid, is deductible.<sup>22</sup> This rule, however, does not apply to lump sum payments of past-due alimony.<sup>23</sup>

Some decrees or instruments provide for monthly payments and, in addition, a special payment of a single large sum upon entry of the decree or upon the occurrence of some contingency. This raises a doubt as to whether the special payment is to be considered a part of a series of periodic payments together with the monthly payments, or whether the special payment is to be considered apart from the monthly payments as a single lump sum payment and, thus, not deductible by the husband.

A separation agreement divided into two separate paragraphs provided that (1) \$15,000.00 was to be paid at \$150.00 per month and (2) guaranteed the difference between the wife's investment income and \$200 per month for the rest of her life after the \$15,000.00 had been paid. The husband contended that both paragraphs should be considered together, making the amount uncertain and the period for payment more than ten years, thus, making the payments deductible. The Tax Court held that the two paragraphs were separate and distinct and, therefore, the payments of \$150.00 per month were not deductible, since they constituted installments of a lump sum payment.<sup>24</sup> If it is necessary to arrange for one or more large payments in addition to monthly payments, it is suggested that the agreement make the larger payment a part of a single series of payments by increasing the monthly payments. For example, \$550.00 per month for the first year and then \$50.00 per month thereafter until the wife's death or remarriage.

The periodic alimony payments must be received by the wife after the date of the decree of divorce or separate maintenance or after the date of the written instrument incident there-

---

<sup>22</sup> Ashcraft, 28 TC 356.

<sup>23</sup> Gale, 23 TC 661.

<sup>24</sup> Hunt, 22 TC 561.

to in order to be deductible by the husband and taxable to the wife.<sup>25</sup>

As a further requirement for deductibility, alimony payments must discharge a legal obligation of support arising out of a family or marital relationship.<sup>26</sup> Nevertheless, the Tax Court held in the case of *Hogg v. Comm.*, 13 TC 361 that periodic payments were deductible by the husband even though the State of Texas imposed no legal obligation upon him to support his wife after divorce. The facts in that case were these. H and W entered into an agreement prior to divorce whereby H was to pay W \$1,200.00 per month. H continued to pay W under the agreement after divorce. The Tax Court held that these payments were deductible, inasmuch as the husband incurred his contractual obligation because of the marital relationship and "to take care of the lack of any provision under law which would require the payment of alimony".

Now let us examine the conclusion reached by the same court in *Fixler v. Comm.*, 25 TC 1313. In this case H and W agreed orally that H would pay W \$50.00 per week for the rest of her life. H then obtained a divorce from W on the grounds of adultery, which under the state law relieved him of his legal obligation of support. He remarried after his divorce and entered into a written agreement with his former wife providing for her support. The court concluded that the periodic payments made by H after divorce were deductible by him as they arose out of an agreement incident to divorce. The court in *Fixler*, it would seem, reached a more reasonable conclusion than it did in *Hogg*.

Another strange conclusion was reached by the Tax Court in the case of *Lehman v. Comm.*, 17 TC 652. Under an agreement incident to a separation and divorce decree, H agreed to pay W \$20,000.00 per year and W's mother \$5,000.00 annually so long as she lived. It was held that the payments made to W's mother arose out of a marital or family relationship and the payments made to her were constructively received by W who had an obligation to support her mother. The payments

---

<sup>25</sup> Sec. 71(a) 1954 IRC; Regs. 1.71-1(b)(1).

<sup>26</sup> Sec. 71(a) 1954 IRC.

to W's mother, the court said, were taxable to W and deductible by H. It would appear doubtful that a husband is obligated to support his mother-in-law. This was the contention of the minority in a strong dissent. The Commissioner, understandably, refused to acquiesce in this case.

If a husband is required by a decree or written instrument incident thereto to repay a loan to his wife, this would not qualify as an alimony payment since it does not arise out of a marital relationship.<sup>27</sup> When periodic payments made by the husband are partly for support and partly in settlement of property rights, it is not too clear that the latter would be deductible as a payment in settlement of a legal obligation arising out of the marital relationship. One circuit court has held that payments settling community property rights are not deductible.<sup>28</sup> The Tax Court has held that payments on a note were not deductible in spite of the husband's testimony that they were in lieu of alimony. It concluded that the note given represented the purchase price of the wife's one-half interest in community property and was not in lieu of alimony as contended.<sup>29</sup> Despite these decisions, the courts might eventually hold that periodic payments made in settlement of inchoate dower rights and rights of inheritance in lieu of dower are obligations arising out of the marital relationship.

Regulations indicate that payments made under an antenuptial agreement later incorporated in a divorce decree or an instrument "incident" to divorce given in consideration of the release of the wife's marital rights (including dower) in the husband's property, and for her support and household expenses, are payments in settlement of a legal obligation resulting from the marital relationship.<sup>30</sup>

The Tax Court has held that an agreement is not "incident" to divorce where there was a lack of intent to divorce at the time the agreement was entered into and the agreement is not

---

<sup>27</sup> Reg. 1.71-1(b)(4).

<sup>28</sup> *Campbell v. Lake*, 220 F(2d) 341; *Scofield v. Greer*, 185 F(2d)551.

<sup>29</sup> *Thompson v. Comm.*, 22 TC 275.

<sup>30</sup> Regs. 1.71-1 (b)(6).

incorporated in the decree.<sup>31</sup> Several circuit courts have held to the contrary. They contend that as long as the legal obligation to support survives the dissolution of the marriage, it is immaterial whether the parties intended the agreement to be "incident" to divorce.<sup>32</sup>

If the husband and wife have an antenuptial agreement providing for her support for life, a divorce decree or written instrument incident thereto referring to that agreement will make the agreement "incident" to divorce. By the same token, any modification of the decree making it refer to the antenuptial agreement would also have the same effect.<sup>33</sup>

An agreement may be "incident" to divorce even though it is not mentioned or incorporated in the decree. This is true even if there is a substantial time interval between the execution of the agreement and entry of the divorce decree.<sup>34</sup> "Incident to" is not "coincident with".<sup>35</sup> A new agreement to continue the support of the wife after remarriage in exchange for the custody of a child has been held "incident" to divorce.<sup>36</sup>

#### IV. GENERAL COMMENTS

Now, a few general observations on the subject of alimony. Alimony payments may be made by cash or out of property transferred to pay alimony. In the latter event, income from the property so transferred is not includible in the income of the husband.<sup>37</sup> Payments made by the husband to reimburse his wife for taxes paid by her on alimony received can constitute additional alimony.<sup>38</sup>

---

<sup>31</sup> Johnson, 21 TC 371.

<sup>32</sup> Holt v. Comm., 226 F(2d) 757; cert. den. 350 US 982; Fineburg v. Comm., 198 F(2d) 260.

<sup>33</sup> Regs. 1.71-1(b)(6) Example 2.

<sup>34</sup> Pease, 26 TC 749.

<sup>35</sup> Macfadden, TCM 1956-287.

<sup>36</sup> Hollander v. Comm., (CCA-9) 10/21/57 rev. 26 TC 827.

<sup>37</sup> Sec. 71(a) 1954 IRC.

<sup>38</sup> Mahana v. US, 88 F Supp. 285; cert den 339 US 978.

It is interesting to note that medical expenses of the wife paid by the husband can qualify as "alimony" and be deductible by him as such. The wife picks up the payment as income but includes it as a medical expense *if* she itemizes her deductions.

Legal expenses incurred by the wife in successfully prosecuting a proceeding for alimony or to increase her alimony are deductible by her as a non-business expense incurred in the production of income, but only to the extent that alimony payments result in taxable income to her.<sup>39</sup> On the other hand, legal fees paid by the husband in defense of such a suit by the wife are not deductible by him. Attorney's fees paid by the husband for the wife in connection with her efforts to increase her alimony are not alimony payments as far as the husband is concerned.<sup>40</sup>

If the wife retains the house formerly occupied by the spouses as a residence, the rental value of the same is not deductible by the husband. If the husband keeps the house and pays the rent on another house for his wife, then the rent paid by him would be deductible as alimony.<sup>41</sup>

The Treasury, I have been advised, has informally indicated that it will allow a deduction for any maintenance expense which the husband is required to pay for his wife, such as transportation, utilities and clothing, even though the amounts are not specified in the decree of divorce or separation. Further, premiums paid by the husband on an insurance policy on his life, irrevocably assigned to his wife, are deductible by him and taxable to the wife.<sup>42</sup> This is not the case where the husband merely names his wife as beneficiary but does not deliver the policy to her, for he could easily change the beneficiary designation as often as he changed his mind. In the case of *Car-michael v. Comm.*, 14 TC 356 the Tax Court held that where the

---

<sup>39</sup> Gale, 13 TC 661.

<sup>40</sup> IT 3856, CB 1947-1, 23.

<sup>41</sup> Gale, 13 TC 661.

<sup>42</sup> IT 4001, CB 1950-1, 27; Stewart, 9 TC 195(A).

purpose of insurance was to provide security for alimony payments, the premiums were not deductible by the husband.

## V. SUPPORT OF MINOR CHILDREN

The portion of any periodic payment designated in a decree, instrument or agreement for support of minor children is not deductible by the husband and is, therefore, not included as income to the wife. If the total payment received by the wife is less than that specified or required, the amount received shall be first considered to be received for the support of the minor children, and only the excess of the amount specified for the minor children is to be included as income to the wife and deductible by the husband.<sup>43</sup> Payments received by the wife for the support of minor children are not deductible by the husband even though he actually supports the children himself in addition to making the payments required.<sup>44</sup>

If no part of the periodic payment is fixed by the decree, instrument or agreement for the support of minor children but is merely received by the wife for her support as well as that of the children, then, the entire amount is includible in the wife's income and deductible by the husband.<sup>45</sup> To express it a little differently, if the amount for the support of the minor children is not fixed, the entire payment is taxable to the wife and deductible by the husband, irrespective of how the money is actually used.<sup>46</sup>

If the amount for the support of the minor children is specified, then the wife does not include this as a part of her income and the same is not deductible by the husband. However, if the amount paid for the support of the minor child represents more than 50% of the total support of that child, then the husband would be entitled to take a deduction in the amount of \$600.00 for the child as a dependent.

---

<sup>43</sup> Sec. 71(b) 1954 IRC; Reg. 1.71-1(e).

<sup>44</sup> Blyth, 21 TC 275.

<sup>45</sup> Reg. 1.71-1(e); Moitoret, 7 TC 640; Hummel, 28 TC 131.

<sup>46</sup> Hummel, 28 TC 131.

Except for amounts designated for the support of minor children, the entire amount of periodic payments received by the wife for her support and that of others, for example, her mother, is includable in her income and deductible by the husband regardless of whether or not the amount for the support of others is specified in the decree, instrument or agreement.<sup>47</sup>

Finally, payments under an oral agreement for arrearages for child support are not alimony and, therefore, not taxable to the wife.<sup>48</sup>

I see that the time allotted for this discussion has expired. It is my hope that what has been said may be of some assistance to all of you, if not personally, then, in your professional capacities.

---

<sup>47</sup> Regs. 1.71-1(e).

<sup>48</sup> Brockel, TCM 1956-243.