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Henry D. Collins
West Virginia University College of Law

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FEDERAL TAXATION OF ALIMONY ARRANGEMENTS

HENRY D. COLLINS

The practicing attorney has been concerned with the Federal Income Tax treatment accorded alimony and support arrangements since section 117 of the Revenue Act of 1942 added, in the main, new sections 22(k), 23(u) and 171 to the Internal Revenue Code. Prior to that time it had been held that the divorced wife receiving alimony need not include any portion of it in her taxable income and, conversely, the alimony-paying divorced husband was allowed no deduction. The Committee Report stated the purpose of the new sections in the following language:

"This section adds new sub-sections . . . in order to provide in certain cases a new income tax treatment for payments in the nature or in lieu of alimony or an allowance for support as between divorced or legally separated spouses. These amendments are intended to treat such payments as income to the spouse actually receiving or actually entitled to receive them and to relieve the other spouse from the tax burden upon whatever part of the amount of such payments is under the present law includible in his gross income. In addition, the amended sections will produce uniformity in the treatment of amounts paid in the nature or in lieu of alimony regardless of variance in the laws of different states concerning the existence and continuance of an obligation to pay alimony."

In the statutory plan devised to carry out this "new income tax treatment", section 22(k) specifies the conditions which must be met in order to make the payments includible in the wife's income. Section 23(u) permits the husband to deduct payments which are includible under section 22(k) in the gross income of his wife. Section 171 provides that a divorced wife shall include in her income the amount of trust income which she is intitiled to receive which normally would be taxable to her husband under section 166 (income from revocable trust taxed to grantor), section 167 (taxing income from trust to grantor where that income may be used for his benefit), or section 22(a) under the rationale of Helvering v. Clifford.

Leaving a consideration of section 171 and its correlation with section 22(k) until a later part of this paper, a discussion of the

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* Assistant professor of law, West Virginia University.
1 56 Stat. 816 (1942).
cases, categorized under the relevant Internal Revenue Code provisions of section 22 (k), should be helpful to the practitioner not especially concerned with federal income tax matters except insofar as they affect his day-to-day practice—in this case divorce and alimony. A sufficient number of cases have been decided, covering such a variety of situations, during the first twelve years of the life of the alimony provisions to provide a beacon to light the way for the practitioner treading the tax path of alimony payments. Admittedly the flame flickers at times and practically dies out to a dull glow on that portion of the path marked "incident to".

A. There must be a decree of divorce or of legal separation and payments must be received subsequent to such decree.

Voluntary payments made prior to the final decree, whether under an oral or a written separation contract are not deductible by the husband under section 23 (u). Nor is a court order or decree entered to enforce the husband's obligation under a voluntary separation agreement sufficient in itself to bring a case within the terms of section 22 (k), for there must have been a decree of divorce or separation and the obligation upon the husband to make payment must have been imposed by that decree or by a written instrument incident to such divorce or separation. Thus, where the husband and wife, in the absence of a decree of divorce or of separation, entered into a private separation agreement whereby he undertook to pay the wife periodic sums for support and his subsequent default compelled the wife to obtain a court order to enforce payment, sums paid by the husband under that enforcement order were not deductible by him under section 23 (u). Payments made to the wife under a court order for separate maintenance are not deductible unless the decree of separate maintenance authorizes the wife to live apart from her husband. It is to be noted that in a suit for separate maintenance under West Virginia Code 48-2-29, the court "may prohibit the husband from imposing any restraint on her personal liberty, and may free her real and personal property from possession, control or any interest of the husband; ...." This language appears to authorize the wife to live apart from her husband, so that, provided there had been

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4 309 U.S. 331 (1940).
5 George D. Wick, 7 T.C. 723 (1946), aff'd, 161 F.2d 732 (3d Cir. 1947).
6 Joseph D. Fox, 14 T.C. 1113 (1950).
7 Charles L. Brown, 7 T.C. 715 (1946); Smith v. Commissioner, 168 F.2d 446 (2d Cir. 1948).
8 Terrell v. Commissioner, 179 F.2d 838 (7th Cir. 1950), cert. denied, 340 U.S. 822 (1950).
a final decree in the case, amounts paid under a decree of separate maintenance in West Virginia should be deductible. However, in practice, a final decree seldom is entered in such causes, the parties usually being satisfied with a *pendente lite* order. Absent a final decree in a West Virginia separate maintenance suit, the payments would be in a nature of temporary or *pendente lite* alimony which are not deductible by the husband nor includible by the wife. In the event the payments have actually been made under a separation contract prior to the actual date of the final decree, they cannot qualify under section 22 (k) even though the final decree is rendered *nunc pro tunc* to the date the payments began.

B. The payments must be "periodic" and cannot be "install-ment" payments of a principal sum.

Although the payments need not be made at regular intervals, they must be "periodic" and installment payments which discharge a part of an obligation the principal sum of which is, in terms of money or property, specified in the decree or instrument are not to be considered periodic payments unless the principal sum, by the terms of the decree or instrument, may be or is to be paid within a period ending more than ten years from the date of the decree or instrument. This provision has created four problems for the Tax Court: (1) What constitutes specification of a principal sum? (2) When a lump-sum is clearly specified, does it become "periodic" because there is also provision for what are otherwise manifestly "periodic" payments? (3) Does payment in a lump-sum of an arrearage in "periodic payments" constitute payment of a "principal sum"? and (4) How to measure the ten year period?

The Tax Court has found an easy solution to the first problem of determining what constitutes specification of a principal sum. In *J. B. Steindel,* the decree specified the payment of $100.00 per month until the sum of $9,500.00 had been paid, unless the wife should remarry and upon her remarriage all remaining payments not in default were to be cancelled. The husband argued that he had only a conditional month-to-month obligation to pay $100.00 to his wife provided she was living and not remarried, the sum of $9,500.00 being merely a maximum limitation upon that obliga-

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9 Frank Kalchthaler, 7 T.C. 625 (1946).
10 George D. Wick, 7 T.C. 723 (1946), *aff'd*, 161 F.2d 732 (3d Cir. 1947); Joseph A. Fields, 14 T.C. 1202 (1950), *aff'd on other issue*, 189 F.2d 950 (2d Cir. 1951); Joseph D. Fox, 14 T.C. 1191 (1950); Robert A. McKinney, 16 T.C. 916 (1951).
12 INT. REV. CODE § 22 (k).
13 10 T.C. 409 (1948).
tion, and this was not an obligation to pay a principal sum such as the statute contemplates inasmuch as the term "obligation" means a definite, unconditional obligation in a specific sum of money. The Tax Court found nothing in legislative history to indicate Congress intended the word "obligation" to mean only absolute, unconditional obligations similar to that represented by a judgment and concluded that Congress must have known that in some states the decrees of courts rendered in divorce actions would differ as to the degree of absoluteness and the lack of contingency in respect to the obligation. The same principle was applied in Frank P. Orsatti Estate,14 where the provision was for payment of $125.00 per week for two years or until the wife remarried or until the wife died, whichever occurred first. The Frank R. Casey15 decree, calling for the payment of the sum of $5,000.00 at the rate of $100.00 per month, met the same fate, the Tax Court pointing out that there was no material difference between a decree where the total amount is expressly set out and one where it is necessary to multiply the weekly payments by the number of weeks over which they are to be paid in order to determine the principal sum specified.

However, where the alimony provision was expressed in terms of a percentage of the husband's future income over a period of less than ten years, the payments were deemed "periodic" because (1) the decree provisions did not fix any total sum as a fixed sum to be paid during the period and (2) the total payments could not be satisfactorily calculated in advance since there was no method of determining what the "net income" of the husband might be.16

The second and third circuits have disagreed with the Tax Court's interpretation of "obligation" insofar as that interpretation ignores the presence of contingencies, the happening of which relieve the husband from making the payments even though the stated period of payment has not expired. In overruling the Tax Court's determination that a principal sum had been specified "by simple arithmetic" where the decree obligated the husband to pay $300 per month for one year and then $200 per month for five years unless the wife had either died or remarried before then, the second circuit court of appeals stated in Baker v. Commissioner:17

14 12 T.C. 188 (1949).
15 12 T.C. 224 (1949).
16 Roland A. Young, 10 T.C. 724 (1948) (percentage of husband's income over 50 month period); John H. Lee, 10 T.C. 834 (1948) (one-third of first $12,000 of husband's income plus 25% of the excess over $12,000 for five years).
17 205 F.2d 369, 370 (2d Cir. 1953), reversing 17 T.C. 1610 (1952).
"We need not decide whether the words 'principal sum' exclude all annuities, even those predictable actuarially, as would be the case here if the sole contingency reducing payments were the wife's death. For here there was the further contingency of the wife's remarriage, and no proof of any actuarial computations in respect of such a contingency. Since a divorced wife's remarriage—in most instances in this respect unlike her death—depends upon some elements of her own seemingly unpredictable choosing, the computation seems to be as far beyond the reach of an educated guess as what will be the first name of the man or woman who will become President of the United States in 1883 . . ."

In Smith's Estate v. Commissioner,18 the husband was required to pay $300 per month for five years and $100 monthly thereafter for the life of the wife or until her marriage, but his liability likewise ceased on his death. In refusing to read into the statute a requirement that the terms of payment must run over ten years in order to be a "periodic" contract, the third circuit held that presence of three contingencies—death of husband, death of wife, remarriage of wife—rendered the promise to pay one which could not be mathematically calculated as a certain obligation of the husband. Therefore, a principal sum had not been specified and the nine $300 per month payments made by the husband during the taxable year were properly deductible.

There was no hint in Smith's Estate as to which contingency was considered most influential. Inasmuch as the second circuit's Baker decision was cited as having been correctly decided, what was said in Baker concerning the feasibility of an actuarial computation of the contingency of the wife's death should likewise apply to the contingency of the husband's death. Therefore, the presence of a provision terminating the husband's liability upon his death, or upon his wife's death, or upon the death of both, should not prevent a mathematical computation of a principal sum in cases of a month-to-month kind of payment plan expressly terminating in ten years or less. The determinative contingency in such cases is that of the wife's remarriage. Apparently that contingency alone is sufficient to avoid specification of a principal sum in this type of alimony plan according to the Baker-Smith's Estate rule.

Naively assuming that the husband's bargaining position with the wife were such that he could enforce upon her such a month-to-month kind of payment plan with an expressed minus ten year termination date, the most recent Tax Court decision on the prob-

18 208 F.2d 349 (3d Cir. 1953).
lem indicates that such a husband will have a very poor bargaining position with the Commissioner. In James M. Fidler, the Tax Court indicated that it would adhere to its J. B. Steindel rule notwithstanding the fact that it has been rejected by the second and third circuits. In the Fidler case the husband was to pay $30,000 in monthly installments of $500.00 over a stated five-year period and, in addition, was to pay $1,620 in monthly installments of $300 over the same stated five-year period except that the $300 monthly installments were subject to a proportionate reduction or elimination should the husband's income from radio contracts be reduced or eliminated in any month during the stated period. In finding a principal sum specified as regards the $300 monthly installments in the Fidler plan, the Tax Court took a position inconsistent with its prior view which gave the "periodic" label to payments measured by a percentage of the husband's future income. There would seem to be as much uncertainty as to the amount of future income in the case where a presently ascertainable income is subject to partial reduction or total elimination by future events as there is in the cases involving percentages of future income. Of course the Fidler case might be distinguished from the percentage-of-future-income cases on the ground that the contingency in the former operated in the manner of a condition subsequent while the contingency in the latter was a condition precedent. Such a distinction based on form has no place in a tax law jurisprudence which insists on realities and substance and takes pride in its ability to discern the essential nature of a transaction.

When the separation agreement or the divorce decree calls for regular month-to-month payments of equal amounts for an indefinite period and, in addition, provides for the payment of larger sums at specific intervals limited in number to occur in ten years or less, the courts have applied a test of "severability" to determine whether or not these larger than ordinary payments are to be treated as simply one of the payments in the string of payments to be made periodically. The Webster New International Dictionary definition of periodic as being "characterized by periods; occurring at regular stated times; happening or appearing, at fixed intervals", has been adopted. Accordingly, in Ralph Norton, where the husband was to pay the wife $200 per month until her death or remarriage and "in addition to said monthly or periodic alimony"
he was to pay her forthwith $5,000 "additional alimony" the $5,000 was held not to be a periodic payment because, (1) the parties themselves did not consider it "periodic", and (2) it was "payable forthwith". However, in affirming Ralph Norton, the eighth circuit rested its decision upon the fact that the $200 per month provision appeared in the decree while the $5,000 lump sum provision was imposed by the voluntary written agreement between the parties, so they were distinct and separate obligations and, being thus separated, the $5,000 could not logically be viewed as merely one of the recurring or periodic payments. Similarly, segregation into separate paragraphs of the separation agreement of the obligation to pay $2,244 over a twelve month period and the obligation to pay "in lieu of alimony" $46.00 per week, enabled the Tax Court to apply its "severability" test to determine that the payment of $46.00 per week was specifically "in lieu of alimony".22 The alimony plan was not "unified" but was "severable" where one paragraph required the husband to pay $500 a month for life and another paragraph required him to pay $45,000 in three $10,000 annual installments and in a final $15,000 installment.23

Although the courts speak in terms of contrasting a "severable" plan with a "unified" plan, no case has been found in which payments of sums larger in amount than the regular month-to-month uniform amount payments have been held to qualify as "periodic" payments. It is conceivable that in the following plan all of the payments would qualify as "periodic": Husband to pay wife $200 per month for eleven months of the year and $1,000 for the twelfth month of the year, the payments to continue for the life of the wife. It will be noted in the example that the $1,000 payable-every-twelfth-month provision is for a period which is not to end or which may not end less than ten years from the date of the decree or the written agreement. If this $1,000 yearly payment were limited for only ten years or less, under the Tax Court test the payments of $1,000 would not be considered "periodic".

Where the wife has received in one lump sum an arrearage of clearly qualified "periodic" payments she has unsuccessfully contended that this was the payment of a principal sum.24 These contentions have caused the courts little difficulty in view of the

23 Edward Bartsch, 18 T.C. 65 (1952), aff'd per curiam, 203 F.2d 715 (2d Cir. 1953).
24 Elsie B. Gale, 13 T.C. 661 (1949), aff'd, 191 F.2d 79 (2d Cir. 1951); Sarah L. Narischkine Estate, 14 T.C. 1128 (1950), aff'd per curiam, 189 F.2d 257 (2d Cir. 1951); Jane C. Grant, 18 T.C. 1013 (1952), aff'd, 209 F.2d 430 (2d Cir. 1953).
specific section 22 (k) provision that payments may be periodic even though they are made at irregular intervals.

If the principal sum specified in a decree or separation agreement is payable in installments or may be paid by installments within a period ending more than ten years from the date of the decree or instrument, then, notwithstanding the specification of a principal sum, the installments are to be treated as periodic, deductible by the husband and includible by the wife. Therefore, it becomes important to determine how the ten year period is to be measured. The husband and wife entered into a written separation agreement on February 27, 1935, providing for the payment of $120,000 in installments over a stated period. The divorce decree was signed by the judge on February 27, 1935, but the order of divorce was not entered until March 2, 1935. Under the particular provisions of the agreement, if the obligation to make the payment arose only upon the entry of the decree as an order on March 2, 1935, the ten year plus period was not satisfied. However, if the obligation became legally binding on the date the agreement was executed or upon the date the judge signed the decree of divorce, then the ten year plus period was satisfied and the installments would be deductible by the husband and includible by the wife. In the case of the wife, the seventh circuit held that the installments were includible in her income because the decree incorporated the prior agreement and made no provision of its own for payment, thus the obligation of the husband to make the payments arose from the agreement and the ten year period begins to run on the date that agreement was executed—February 27th.25 In the case of the husband, the seventh circuit held that he could deduct the payments because under Illinois law a judgment becomes effective as soon as it is pronounced and not from the time it is entered as an order, therefore, the February 27th date was determinative.26

C. Payments must discharge a legal obligation which, because of the marital or family relationship, is imposed upon or incurred by husband under the divorce decree or under a written instrument incident to such divorce or separation.

The Tax Court has been lenient in enforcing the requirement that there be a written instrument creating the legal obligation of the husband in the absence of provisions for alimony in the decree

26 Harry Blum v. Commissioner, 177 F.2d 670 (7th Cir. 1949), reversing 7 T.C.M. 798.
itself. Informal correspondence between the parties prior to the divorce wherein the husband agrees to pay for support and maintenance will suffice.\textsuperscript{27} So long as the separation agreement expressly\textsuperscript{28} provides for payments for the wife's support and maintenance and satisfies the controversial requirement of being "incident to" the divorce decree, it matters not that state law does not allow alimony in an absolute divorce,\textsuperscript{29} nor that state law does not impose a duty of support upon the divorced husband.\textsuperscript{30} However, the fact that state law does provide for alimony after divorce has been helpful in avoiding a determination that the payments called for in the separation agreement were in reality the purchase price of a property interest transferred by the wife.\textsuperscript{31} The legal obligation imposed by the separation agreement and discharged by the payments provided thereunder must be the marital obligation to support the wife and cannot be a contractual obligation to purchase property interests of the wife.\textsuperscript{32}

When the obligation to make alimony payments is imposed upon the husband by a written separation agreement rather than by the divorce decree, it is essential that the written instrument be "incident to such divorce or separation." The most serious problem posed by the alimony sections of the Code has been that of ascertaining what is meant by "incident to". On the basis of their facts, the cases may be divided into two classes, (1) those involving pre-divorce agreements and (2) those involving post-divorce agreements.

(1) \textit{Pre-divorce agreements}. In the first class of cases the common fact is that a written separation agreement has been entered into prior to the divorce action and the problem is whether the statute requires that one or both of the parties must have definitely anticipated or contemplated obtaining a divorce at the time the agreement was executed. In other words, does "incident to" mean "in contemplation of"? If it does, must the contemplation be of specific action or will a general contemplation suffice?

The Tax Court viewpoint insists that both parties must contemplate taking specific action to obtain a divorce at the time they

\textsuperscript{27} Floyd W. Jefferson, 18 T.C. 1092 (1949); Charles Campbell, 15 T.C. 355 (1950).
\textsuperscript{28} Ben Myerson, 10 T.C. 729 (1948) (written separation agreement covered only custody of children and made no mention of payments for wife's support).
\textsuperscript{29} Tuckie G. Hess, 7 T.C. 700 (1946) (Pennsylvania law).
\textsuperscript{30} Thomas E. Hogg, 13 T.C. 361 (1949) (Texas law); Floyd H. Brown, 16 T.C. 693 (1951) (Louisiana law).
\textsuperscript{31} Julia Nathan, 19 T.C. 865 (1952).
\textsuperscript{32} Frank Dubane, 10 T.C. 992 (1948).
execute the written separation agreement. The fact that one spouse may be considering the possibility of a divorce is not enough to make the agreement "incident to" a divorce later obtained.\textsuperscript{33} Moreover, it is not sufficient that the parties considered the possibility of divorce at some unspecified time.\textsuperscript{34} Originally this Tax Court mutual contemplation doctrine was invoked to excuse omission from the divorce decree of any mention of the prior written agreement.\textsuperscript{35} So long as the requisite mutual contemplation was present, it mattered not that nothing was said in the separation agreement about divorce,\textsuperscript{36} or that the separation agreement was not made specifically contingent upon obtaining a decree,\textsuperscript{37} in recognition of the danger of a charge of collusion. Because of the Tax Court contemplation rule, a plausible explanation must be offered where a long interval of time elapses between the date of the agreement and the date of the decree.\textsuperscript{38} However, the fact that the separation agreement provides that it might be incorporated into any subsequent divorce decree obtained will not suffice to show the presence of the requisite contemplation where there is evidence that the wife consistently refused either to obtain a divorce or to consent to husband's obtaining one.\textsuperscript{39}

The circuit\textsuperscript{40} and district\textsuperscript{41} courts have been unanimous in their rejection of the Tax Court's contemplation test in cases of pre-divorce separation agreements. Reasons assigned for the rejection of the contemplation test are three-fold: (1) it posed a dilemma for attorneys in states where the divorce might be voided by collusion; (2) a party's state of mind during periods of emotional stress attendant upon the break-up of a marriage is not generally subject to objective proof, and (3) the term "written instrument incident to such divorce" was designed only to insure proof of the

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\item \textsuperscript{33} Cecil A. Miller, 16 T.C. 1010 (1951), rev'd 199 F.2d 597 (9th Cir. 1952).
\item \textsuperscript{34} George J. Feinberg, 16 T.C. 1485 (1951), rev'd 198 F.2d 260 (3d Cir. 1952).
\item \textsuperscript{35} Jessie L. Fry, 13 T.C. 658 (1949).
\item \textsuperscript{36} Robert W. Johnson, 10 T.C. 647 (1948).
\item \textsuperscript{37} George T. Brady, 10 T.C. 1192 (1948).
\item \textsuperscript{38} George T. Brady, 10 T.C. 1192 (1948) (lawyers were busy and unable to secure necessary documents); Bertram G. Zilmer, 16 T.C. 365 (1951) (eighteen months' time interval explainable where husband did not have sufficient funds to finance an immediate divorce action); Jessie L. Fry, 13 T.C. 658 (1949) (two year interval because wife reneged on original promise to secure immediate divorce).
\item \textsuperscript{39} Florence B. Moses, 18 T.C. 1020 (1959).
\item \textsuperscript{40} Israff v. Commissioner, 193 F.2d 625 (2d Cir. 1952), affirming 15 T.C. 573 (1950); Lerner v. Commissioner, 195 F.2d 296 (2d Cir. 1952), reversing 15 T.C. 579 (1950); Feinberg v. Commissioner, 198 F.2d 260 (3d Cir. 1952), reversing 16 T.C. 1485 (1951); Commissioner v. Miller, 199 F.2d 597 (9th Cir. 1952), reversing 16 T.C. 1010 (1951).
\item \textsuperscript{41} Stewart v. Rothensies, 114 F. Supp. 497 (E.D. Pa. 1953).
\end{itemize}
existence of the obligation when divorce has occurred.42 Other reasons, unstated, but equally compelling, are: (1) a divorced wife, as an interested party, might well be tempted to perjure herself because of the tax savings ensuing to her from a finding that she had not contemplated divorce at the time she signed the separation agreement; and (2) interspousal income splitting has been permitted since 1948, so there is no longer need to guard against attempts to shift income between spouses. Logical as these reasons for non-recognition of the contemplation test may be, the Tax Court has recently indicated an intention to continue applying it.43

(2) Post-divorce agreements. When the husband enters into a post-divorce agreement, can he be said to be discharging a legal obligation arising from the marital or family relationship when the support obligation has already once been satisfied by a pre-decree agreement or by provisions of the divorce decree? Can there be any legal obligation arising from the marital or family relationship remaining once a valid divorce decree is entered which makes no provisions for alimony and there has been no pre-divorce agreement on the matter? These are the problems facing the courts in cases of post-divorce agreements. Here the case language is more apt to emphasize the "legal obligation" approach rather than the "incident to" approach.

The Tax Court, supported by the court of appeals for the District of Columbia and the third circuit court of appeals, takes the firm stand that the phrase "written instrument incident to such divorce" should be read "written instrument incident to such divorce decree" rather than "written instrument incident to such divorce status" (italicized words added). Accordingly, increased payments made to the wife under a post-divorce agreement, the pre-divorce agreement not having been incorporated into the decree and no jurisdiction having been retained by the divorce court, were not deductible by the husband.44 Nor can a post-divorce modification of a pre-divorce agreement not incorporated into the decree be "incident to" the divorce, especially when the modifying post-divorce agreement is executed fourteen years after the decree.45 Where there was no pre-divorce agreement and no provision in the decree for alimony, a post-divorce agreement made seven

42Lerner v. Commissioner, 195 F.2d 296 (2d Cir. 1952), reversing 15 T.C. 379 (1950).
43Florence B. Moses, 18 T.C. 1020 (1952).
44Frederick S. Dauwalter, 9 T.C. 580 (1947).
months later to preserve the divorced status by dissuading the wife from collaterally attacking the divorce is not "incident to" such divorce inasmuch as the divorce terminated his marital obligation.\(^{46}\) Under these cases the fact that the parties have the status of being divorced at the time the post-divorce agreement is executed is insufficient to make that agreement "incident to the divorce", "such divorce" being interpreted to mean "such divorce decree".

There are strong intimations in the language of decisions in the second and first circuits and the court of claims that "incident to such divorce" may indeed mean "incident to such divorce status". Although finding that the decretal obligation to support survived the private post-divorce modification under state law, the second circuit was "not prepared to say" that the phrase "incident to such divorce" should be read as "incident to such divorce decree" in Commissioner v. Murray.\(^{47}\) There the wife was unable to prove that she had received payments under the private post-divorce agreement in excess of those provided in the decree and since the decree was still a legally enforceable obligation of the husband, payments made by him, to the extent of the amount specified in the decree, were includible in her income under section 22 (k).

In Smith v. Commissioner\(^{48}\) the first circuit felt "that in view of the purpose of section 22 (k) to secure tax uniformity irrespective of variances in state laws . . . there is much to be said for reading the phrase 'written instrument incident to such divorce' as referring to the continuing status of the legal obligation to support the divorced spouse." In Smith the pre-divorce agreement specifically left open the final settlement of the support question and was incorporated in that form into the decree. Thus the decree, too, left open until a later time the final settlement of the support question. Accordingly, when six years later the parties negotiated a final settlement of the alimony question pending an appeal by the husband for alimony reduction and had the husband's appeal dismissed under a final decree eliminating alimony in view of the wife's acceptance of the settlement, the court logically found that the origin or motive for the post-divorce agreement could be traced to no other obligation than the one arising from a family or marital relationship. Similarly, in DuPont v. United States,\(^{49}\) where the divorce court had continuing jurisdiction in the sense that it had

\(^{46}\) Cox v. Commissioner, 176 F.2d 226 (3d Cir. 1949), affirming 10 T.C. 955 (1948).

\(^{47}\) 174 F.2d 816 (2d Cir. 1949), affirming 7 T.C.M. 365.

\(^{48}\) 192 F.2d 841 (1st Cir. 1951), affirming 16 T.C. 639 (1951).

\(^{49}\) 104 F. Supp. 978 (Ct. Cl. 1952).
power to annul its alimony provisions on the ground of false representation, a post-divorce compromise agreement executed to forestall the possibility that the wife would seek an annulment of the decree on that ground is a written agreement incident to the original divorce decree.

It is to be noted that the Smith and DuPont cases, the outstanding examples recognizing post-divorce agreements, involved situations where (1) the husband was still under a legal obligation of support at the time he made the post-divorce modifying agreement and (2) the divorce court still had jurisdiction of the divorce action, either expressly or through power to modify because of fraud. These circumstances may limit the scope of recognition which will be given to post-divorce agreements under section 22 (k). One writer\textsuperscript{50} and a district court\textsuperscript{51} have characterized the Smith and Murray cases as indicating the trend of decisions is headed to a holding that "any revision will satisfy the legal obligation requirement if the original agreement was executed while a legal obligation to support existed." Another writer\textsuperscript{52} feels that the acceptance of the Smith approach will mean that "any post-divorce agreement for the separate maintenance of the wife executed while the husband is still obligated to support will be considered incident to the divorce, irrespective of whether the divorce decree is modified to incorporate the agreement."

In its very latest decision on the subject, the Tax Court has indicated that it will now recognize payments made under a post-divorce revision of a pre-divorce contract even though the pre-divorce contract was not enforceable under state law because not incorporated into the decree.\textsuperscript{52a} Since this post-divorce contract was a revision of the original agreement executed while the parties were still married with the husband under the legal obligation of support, this decision appears to be the holding prophesied from an analysis of the trend of decisions by the court and writers as outlined in the preceding paragraph.

D. Support of minor children.

Section 22 (k) does not apply to that part of the periodic payment which the terms of the decree or written instrument fix, in terms of an amount of money or a portion of the payment, as a sum which is payable for the support of minor children of the

\textsuperscript{50} Comment, 61 Yale L.J. 1200 (1952).
\textsuperscript{52} Baum, What Is "Incident" to a Divorce: The Problem of Section 22 (k), N.Y.U. Twelfth Annual Institute on Federal Taxation 508, at 521 (1953).
\textsuperscript{52a} Raoul Walsh, 21 T.C. ——, No. 120 (March 31, 1954), CCH Dec. 20, 289.
husband. In the event any periodic payment is less than total amount specified in the decree or written instrument, it is to be applied first to the satisfaction of the sum payable for the support of the minor children. In other words, the husband is not entitled to deduct, nor is the wife required to include in her income, that portion of the periodic payment which the decree or agreement specifies to be payable for support of minor children, partial payments being applied first against the amount specified for support of minor children.

As might be imagined the cases all deal with the question, What amounts to specification of a sum payable for support of minor children? Here again the test is couched in terms of "severability", that is, construing the agreement or decree as a whole, reading each paragraph in the light of the other paragraphs, can it be said that any amount, in terms of dollars or portions, is "allocable" to child support and thus "severable" from the payments for the wife's support and maintenance?

If no allocable amount is specified for child support, the fact that the wife did not want any part of it for herself and actually used it all for the children is immaterial. Provisions for reduction (in dollars, fractions or percentages) of the lump sum monthly payment upon the death or remarriage of the wife or upon the death of a child or upon the child's obtaining majority constitute sufficient specification of child support payments. Absent the requisite specification in the original decree, amendments nunc pro tunc cannot have retroactive effect.

Even though the decree specifies a "severable" sum for child support, the husband must still prove that he supplied over one-half of the actual cost of support in order to be entitled to an exemption for the child. However, the fact that support money is not actually used for the child's support is immaterial so long as the husband's child support payment is in excess of one-half of the actual cost of such support.

53 Dora H. Moitoret, 7 T.C. 640 (1946).
54 Warren Leslie, Jr., 10 T.C. 807 (1948).
55 Robert W. Budd, 7 T.C. 413 (1946), aff'd, 177 F.2d 198 (6th Cir. 1947).
56 Harold M. Fleming, 14 T.C. 1308 (1950); Mandel v. Commissioner, 185 F.2d 50 (7th Cir. 1950).
57 Robert W. Budd, supra note 56.
58 Edna M. Gilbertson, 10 T.C.M. 594 (1951).
59 See Donald A. Hansaker, 11 T.C.M. 1184 (1952). In the vast majority of cases the husband is unable to prove the total cost of support because that information is possessed by an adverse party—the wife who likewise desires to use the dependency exemption.
60 I.T. 9883, 47-2 CUM. BULL. 38.
E. Alimony payments from property transferred (in trust or otherwise) in discharge of legal obligation imposed upon or incurred by husband under decree or "incident" written instrument.

Often an alimony plan will provide a definite source for the periodic payments by requiring that the husband transfer an income-producing property either directly to the wife, or in trust for the wife. On the other hand, long prior to the divorce, either as part of the ante-nuptial agreement or otherwise, the husband may have created a trust for the benefit of the wife or assigned a beneficial interest to her; and when the marriage ends up in divorce proceedings no provisions are made in the decree or in the written separation agreement concerning alimony because it is felt the previously created trust or assigned beneficial interest will continue to supply the wife with sufficient income for her support. Section 22 (k) covers the former situation and section 171 covers the latter situation.

Section 22 (k) will always apply when a transfer of property is made, or a trust is originally created, or an assignment of a beneficial interest in a previously created trust is made, to discharge the legal support obligation specified in the decree or "incident" written instrument.\(^1\) Section 22 (k) also covers previously created trusts or previously assigned beneficial interests if payments to the wife under the trust continue in discharge of the legal support obligation specified in the decree or "incident" written instrument.\(^2\) Section 171 can never apply to any trust to which section 22 (k) is applicable.\(^3\) Accordingly, section 171 is usually applicable to trusts in which the divorced wife has a beneficial interest derived from the husband where there is no legal obligation of support imposed upon the husband by the decree or "incident" written instrument and the trust was not created, nor the assignment of a beneficial interest to the wife made, in contemplation of divorce.

If either section 22 (k) or 171 is applicable to the trust, the trust income is includable in the divorced wife's income and excludible from the husband's income even though the husband would otherwise ordinarily be taxable on the trust income either because (1) he retains a power to revoke,\(^4\) or (2) he retains an interest in the
trust income,\textsuperscript{65} or (3) he retains a control over the trust so complete that he is still in practical effect the owner of its income.\textsuperscript{66} However, the chief distinction between the application of sections 22 (k) and 171 to the alimony trust lies in the fact that if section 22 (k) is applicable the wife must include in her income the full amount of periodic payments received attributable to the property in trust, whether or not out of trust income.\textsuperscript{67} On the other hand, section 171 requires amounts paid, credited or to be distributed to her to be included in her income only to the extent such amounts are out of income of the trust for its taxable year.\textsuperscript{68} Therefore, if section 22 (k) is applicable a distribution of trust corpus to the wife in the form of a periodic payment would be taxable income to her.

Insofar as the trust instrument or decree fixes in terms of an amount of money or a portion of trust income, a sum which is payable for support of minor children of the husband, neither section 22 (k) nor 171 is applicable to such amounts of trust income.\textsuperscript{69} The wife will not include such sums in her income and the husband usually must include such sums in his income under section 167.

The chief advantage in using the alimony trust arises from the fact that the husband can retain a great deal of control over the trust res during the life of the wife and recover it entirely upon her death without being taxed on the trust income in the interval. Therefore, the trust device is preferable in situations where an out and out transfer of assets in a lump sum settlement would deprive the husband of some economic advantage, other than the receipt of direct income, growing out of ownership of the assets. The most common example is controlling stock in a closed corporation.

F. Miscellaneous matters.

(1) Life insurance in alimony arrangements. Often the alimony plan involves an assignment of existing life insurance policies to the wife. Two tax questions arise from such an arrangement. (1) Can the husband deduct, and must the wife include, amounts thereafter paid by the husband in the form of insurance premiums? (2) Will the wife be taxed upon the proceeds of the assigned policy?

\textsuperscript{65} \textit{Int. Rev. Code} \S 167.
\textsuperscript{66} \textit{U.S. Treas. Reg.} 118, \S 39.22 (a)-21. (The Clifford regulations).
\textsuperscript{67} \textit{U.S. Treas. Reg.} 118, \S 39.171-1.
\textsuperscript{68} \textit{Supra} note 67.
\textsuperscript{69} \textit{Int. Rev. Code} \S\S 22 (k) and 171 (a).
In order that the insurance premiums paid by the husband be entitled to the classification of "periodic payment", it is essential that the policy be absolutely assigned to the wife and that she be irrevocably designated as primary beneficiary. If it is possible to interpret the assignment of the policy as being only security for the payment of alimony, the premiums paid are not "periodic payments". If the decree prohibits the husband from changing, at any future time (emphasis added), the designation of the wife as primary beneficiary, then premium payments are deductible. However, if the restriction on change of beneficiary is to continue only during the wife's life so that the husband would regain full possession and control of the policy in the event she predeceased him, the premium payments are not deductible by the husband inasmuch as they are not paid for the sole benefit of the divorced wife.

The proceeds of a life insurance contract paid by reason of the death of the insured are exempt from federal income taxes, unless there has been an assignment of the policy for a valuable consideration. Accordingly, although there are no cases, insofar as the wife accepts the irrevocable assignment of the policy in divorce proceedings in consideration of her release of the marital rights of support, she should be taxed on the proceeds of the policy. This result can be avoided by taking out a new policy rather than assigning existing policies if age, cost and other factors permit.

(2) Deductibility of legal expenses. The original Treasury viewpoint disallowed a deduction for legal fees paid either to secure alimony or to resist an attempt to secure alimony. The cases have denied a deduction for attorney fees paid by the wife to secure the divorce, but have permitted her to deduct legal fees paid to secure a lump sum settlement of periodic payments or to secure an increase in alimony for both past and future years. The husband cannot deduct legal fees paid in defending the wife's suit to collect alimony arrearages, for the payment is not ordinarily

70 I.T. 4001, 1950-1 CUM. BULL. 27; Anita Quimby Stewart, 9 T.C. 195 (1947).
71 Lemuel A. Carmichael, 14 T.C. 1356 (1950); Blumenthal v. Commissioner, 183 F.2d 15 (8d Cir. 1950).
72 Lemuel A. Carmichael, 14 T.C. 1356 (1950).
73 Smith's Estate, 11 T.C.M. 1167 (1958).
74 INT. REV. CODE § 22 (b) (1).
75 INT. REV. CODE § 22 (b) (2).
76 I.T. 3856, 1947-1 CUM. BULL. 23.
77 Barbara B. Lemond, 19 T.C. 670 (1949).
78 supra note 77.
79 Elsie B. Gale, 13 T.C. 661 (1949), aff'd, 191 F.2d 79 (2d Cir. 1951). The Treasury has accepted the decision. See Treas. Reg. 118, § 39.23 (a)-1.
related to a business activity.\textsuperscript{80} Nor is it material that under state law the wife could have sequestered his property to secure her demand for arrearages.\textsuperscript{81} However, where there was a showing that part of the legal fee paid by the husband in connection with a separation agreement was allocable to successful compromise of a claim made by the wife which would have caused the husband to lose control of property from which he derived his income, deduction of such allocable part of the fee was permissible under section 23 (a) (2) as an expense incurred for the management, conservation or maintenance of property held for the production of taxable income.\textsuperscript{82}

G. \textit{Internal Revenue Code of 1954}.

As of the date this article was written, the House of Representatives had passed its version of the \textit{Internal Revenue Code of 1954}.\textsuperscript{83} Section 71 of the H.R. 8300 generally corresponds to section 22 (k) of the \textit{Internal Revenue Code of 1939} except for the insertion of the following paragraph:

"If a wife is separated from her husband and there is a written separation agreement, the wife's gross income includes periodic payments (whether or not made at regular intervals) received after such agreement is executed which are made under such agreement and because of the marital or family relationship (or which are attributable to property transferred, in trust or otherwise, under such agreement and because of such relationship). This paragraph shall not apply if the husband and wife make a single return jointly."

The Committee Report finds\textsuperscript{84} that present treatment discriminates against husbands and wives who have separated although not under a court decree and states\textsuperscript{85} that no substantive change, except for that contained in the quoted paragraph, has been made in the 1939 Code section 22 (k) provision.

If the Senate accepts the House version of new section 71, the uncertainties concerning pre-divorce agreements should disappear. The "contemplation" test will no longer be needed. The new Tax Court view\textsuperscript{86} on post-divorce revisions of pre-divorce agreements will do much to free post-divorce agreements from tax litigation.

\textsuperscript{80} Lindsay C. Howard, 16 T.C. 157 (1951), aff'd, 202 F.2d 28 (5th Cir. 1953).
\textsuperscript{81} Thorne Donnelley, 16 T.C. 1196 (1951).
\textsuperscript{82} Baer v. Commissioner, 196 F.2d 646 (8th Cir. 1952), reversing 16 T.C. 1418 (1951).
\textsuperscript{83} H.R. 8300, 83d Cong., 2d Sess.
\textsuperscript{86} Supra note 52a.
However, absent a pre-divorce contract or a decreed support obligation, it is doubtful if a post-divorce agreement will qualify without further statutory modification. *Cox v. Commissioner* should remain good law in this respect.

Future tax litigation in the alimony area can be expected in the main to be limited to purely interpretative decisions in the "periodic versus installment" and "child support" fields and to clarifying determinations of the effect of contingencies upon the specification of a principal sum.