

Fox Rothschild Podcast

Featuring New Jersey Family Law Attorneys Robert Epstein and Eliana Baer in Princeton

We are talking today with Robert Epstein and Eliana Baer on Fox Rothschild Podcast. Our topic is the tax deduction of alimony, and specifically, why it is critical to structure a divorce or settlement agreement that leaves no ambiguity regarding deduction in the eyes of the IRS.

Robert and Eliana are attorneys with the firm's New Jersey Family Law Group. They are frequent contributors to the firm's New Jersey Family Legal Blog and helped to develop the firm's New Jersey Divorce app for mobile devices. Robert, Eliana, good morning.

Robert Epstein and Eliana Baer: Good morning. Thank you.

Question: *The IRS does allow a spouse to deduct alimony payments, does it not?*

Eliana Baer: Yes. The Internal Revenue Code specifically sets forth that the spouse who is paying the alimony may deduct a taxable year's worth of payments to the extent that those payments are included in the recipient spouse's gross income.

Robert Epstein: The IRS defines alimony as any cash payment that is received by a spouse under a divorce or separation agreement that does not stipulate that the payment is neither includible in gross income nor allowable as a deduction. It also notes that the payor and recipient spouses must not be members of the same household when payments are made, and that payment obligation ceases upon the death of the recipient spouse.

Eliana Baer: But, there is a catch.

Question: *What's the catch?*

Eliana Baer: Well, the Code provides that if the alimony payments are subject to "any contingencies involving a child," then the payment is considered payment made for the child and is not deductible. So, for example, a child leaving school may be one such contingency.

Robert Epstein: And this is true even if there is a specifically defined, clearly articulated and separately allocated child support payment noted in the divorce or separation agreement, and that payment is being made by the payor spouse.

***Question:** Interesting. So if this is defined so clearly by the IRS, then there shouldn't be any issues surrounding whether alimony is deductible.*

Robert Epstein: You would think so, but because divorce and settlement agreements are sometimes poorly constructed, there can be. Recently, the U.S. Tax Court ruled that a former husband was unable to deduct payments made to his ex-wife as alimony because the parties' divorce agreement stipulated that "spousal maintenance" payments would end when one of several events occurred, one of which was the graduation from high school of the youngest child. The core issue in this case was whether the payments, in the eyes of the IRS, constituted alimony payments or child support payments.

***Question:** I can see how that might have been interpreted by the IRS as a contingency, given the way the agreement was worded.*

Eliana Baer: Yes, and in this particular case, the settlement agreement between the spouses also provided for a separate child support payment in addition to the spousal maintenance payments and expressly noted the spousal maintenance payments would be tax-deductible by the husband and taxable to the wife. Both parties abided by the agreement in completing their respective tax returns subsequent to the divorce.

***Question:** Well that certainly seems to comply with the IRS Code that the payments would have been non-deductible, given the way you're previously explained the Code.*

Robert Epstein: Yes, and the husband argued that the graduation date was intended as a reference point for the termination of alimony. But the IRS apparently doesn't acknowledge "reference points." It said that intent "holds no value" and concluded that the payments were in fact a form of child support, rather than spousal support, at least as far as tax deductions go.

***Question:** So the takeaway here is that agreements need to remove any potential ambiguity?*

Eliana Baer: Indeed. This case serves as a cautionary tale for litigants and for matrimonial attorneys. When structuring agreements, do not use language similar to that used in the parties' agreement in this case when defining alimony.

Robert Epstein: Similar to this case here, I've seen many clients' settlement agreements drafted by other attorneys that use a child's achievement of a milestone – such as graduation from school, when the child reaches a certain age, etc. – as the termination date for alimony payments. That leaves the payor spouse open to great risk of losing the tax deduction, like what happened here.



Eliana Baer: The risk of losing the tax deduction by using such language can prove disastrous. We advise that spouses be safe and ensure the terms of alimony payments are defined through the use of specific dates, which leave no ambiguity in the eyes of the IRS.

Narrator: Well, thank you, Robert and Eliana. Listeners, to confidentially discuss the tax deduction of alimony payments or the structuring of divorce or settlement agreements, please contact Robert Epstein in Roseland, New Jersey at 973.994.7526 or Eliana Baer in Princeton at 609.895.3344.

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