

## ***Brady v. Commissioner, 10 T.C. 1192 (1948)***

A written separation agreement is considered “incident to divorce” under Section 22(k) of the Internal Revenue Code if it is part of a process where divorce was contemplated by the parties when the agreement was executed, even if the agreement doesn’t explicitly require a divorce or is not directly referenced in the divorce decree.

### **Summary**

The Tax Court addressed whether payments made under a separation agreement were deductible by the husband as alimony. The court held that the agreement was “incident to divorce” because the evidence showed that both parties contemplated divorce when the agreement was executed. This conclusion was reached despite the fact that the agreement didn’t explicitly mention divorce, nor was it referenced in the divorce decree. The court emphasized that the intent to avoid collusion should be considered when determining the relationship between agreements and divorce proceedings. Therefore, the payments were deductible by the husband and taxable to the wife.

### **Facts**

The petitioner, Mr. Brady, and his wife, Hazel, separated. Mr. Brady desired a divorce for at least five years prior to October 1937. On October 30, 1937, they executed a separation agreement that provided for monthly payments of \$200 from Mr. Brady to Hazel. Mr. Brady refused to sign the agreement unless a divorce action was initiated. Hazel later obtained a divorce in Massachusetts. The divorce decree did not refer to the separation agreement.

### **Procedural History**

The Commissioner of Internal Revenue disallowed Mr. Brady’s deductions for the payments made to Hazel under the separation agreement. Mr. Brady petitioned the Tax Court for a redetermination of the deficiency. The Tax Court reviewed the case to determine if the payments qualified as deductible alimony payments under Sections 22(k) and 23(u) of the Internal Revenue Code.

### **Issue(s)**

Whether the separation agreement providing for monthly payments to the petitioner’s divorced wife was executed “incident to divorce” under Section 22(k) of the Internal Revenue Code, thus making the payments deductible by the husband under Section 23(u).

### **Holding**

Yes, because the conduct and statements of the petitioner and his wife’s counsel, the

sequence of events, and the terms of the agreement itself, all indicated that the agreement was executed in contemplation of divorce and was, therefore, incident to the divorce.

### **Court's Reasoning**

The court relied on the intent of Section 22(k) to tax alimony payments to the divorced wife. The court found the payments to be in the nature of alimony. It emphasized that the petitioner had desired a divorce for a long time prior to the agreement, and he insisted on the initiation of divorce proceedings before signing the agreement. Although the agreement did not explicitly require a divorce, the court acknowledged that this was likely to avoid the appearance of collusion, which is prohibited by public policy: "The rule is well established that any agreement, whether between husband and wife or between either and a third person, intended to facilitate or promote the procurement of a divorce, is contrary to public policy and void." The court distinguished other cases cited by the Commissioner, finding the facts sufficiently different. The court found the divorce itself to be the vital factor, rather than the specific jurisdiction where the divorce action was filed.

### **Practical Implications**

This case clarifies that the phrase "incident to divorce" under Section 22(k) (and its successor provisions) is not limited to agreements explicitly conditioned on divorce or incorporated into the divorce decree. The focus is on whether the agreement was part of the process leading to the divorce. Attorneys drafting separation agreements should be aware that even if the agreement is silent on divorce, the surrounding circumstances can establish that it was incident to a divorce. This affects the tax treatment of the payments, making them taxable to the recipient and deductible by the payor. This case is often cited in disputes over the tax treatment of spousal support payments, particularly when the agreement's connection to the divorce is not explicitly stated. Later cases have further refined the analysis of "incident to divorce," often looking at the timing of the agreement relative to the divorce proceedings and the degree to which the agreement resolves marital property rights.