18 T.C. 65 (1952)

Payments made pursuant to a divorce decree are considered 'installment payments' (and thus not deductible by the payor) when they discharge a specific principal sum outlined in the decree, as opposed to 'periodic payments' intended for ongoing support.

Summary

Edward Bartsch sought to deduct payments made to his former wife, Sarah, under a divorce decree, claiming they were alimony. The decree incorporated a separation agreement specifying monthly payments for Sarah's lifetime or until remarriage, and a fixed sum of $45,000 to be paid in installments. The Tax Court disallowed deductions for the $10,000 payments made in 1946 and 1947, holding they were 'installment payments' discharging a principal sum and not deductible as alimony. The court emphasized that the parties' agreement clearly distinguished between periodic support payments and the fixed-sum obligation.

Facts

Edward and Sarah Bartsch entered into a separation agreement on June 29, 1946, stipulating: (1) Edward would pay Sarah $450 monthly for life or until remarriage; and (2) Edward would pay Sarah $45,000 in installments ($10,000 in 1946, 1947, 1948 and $15,000 in 1949). The agreement was made in contemplation of divorce and stipulated that its terms should be incorporated into any divorce decree. A Florida divorce decree, issued on August 19, 1946, ratified the separation agreement and ordered Edward to make the payments as specified. Edward paid Sarah $10,000 in 1946 and $10,000 in 1947, which he deducted as alimony. Sarah did not report these payments as income.

Procedural History

The Commissioner of Internal Revenue disallowed Edward's deductions for the $10,000 payments made in 1946 and 1947. Edward Bartsch petitioned the Tax Court for a redetermination of the deficiencies assessed by the Commissioner.

Issue(s)

Whether payments made by Edward to Sarah under the divorce decree constituted deductible "periodic payments" or non-deductible "installment payments" under Sections 22(k) and 23(u) of the Internal Revenue Code.

Holding

No, because the $10,000 payments in 1946 and 1947 were considered installment payments discharging a principal sum specified in the separation agreement and divorce decree. As such, they are not deductible under Section 23(u) of the Internal

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Revenue Code.

Court’s Reasoning

The Tax Court reasoned that the separation agreement, later incorporated into the divorce decree, clearly distinguished between two types of payments: periodic monthly payments for Sarah’s ongoing support and a lump-sum obligation of $45,000 payable in installments. The court emphasized that had the agreement only contained the provision for the $45,000, those payments would clearly be considered installment payments not subject to deduction. The court rejected the argument that the divorce decree represented a unified plan for alimony, stating that the parties themselves differentiated the payments in the original agreement. The court noted, “The plan of payment may have been a single plan, but we do not think that requires us to press the payments under both paragraphs in the same mold when the parties themselves have differentiated them.” Therefore, the court concluded that the monthly payments were deductible periodic payments, while the installment payments towards the $45,000 principal sum were not deductible.

Practical Implications

This case clarifies the distinction between periodic and installment payments in divorce settlements for tax purposes. Attorneys drafting separation agreements and divorce decrees must carefully delineate the nature of payments to ensure the intended tax consequences for their clients. Specifically, if a lump-sum payment is intended, it should be clearly separated from periodic support payments to avoid being classified as deductible alimony. This case serves as a reminder that the form of the agreement, as defined by the parties, will be respected unless there is a compelling reason to collapse separate provisions. Later cases may distinguish Bartsch if the payment schedule extends beyond ten years, potentially qualifying the payments as periodic even if a principal sum is specified.

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