Grant v. Commissioner, 18 T.C. 1024 (1952)

Lump-sum payments of alimony arrearages retain the character of periodic payments and are taxable as income to the recipient and deductible by the payor.

Summary

Jane C. Grant received a lump-sum payment of $10,720 from her former husband, Harold W. Ross, representing accumulated alimony arrearages from a 1929 separation agreement that was incident to their divorce. The Commissioner of Internal Revenue inconsistently determined that the payment was taxable income to Grant but not deductible by Ross. The Tax Court addressed whether this lump-sum payment constituted "periodic payments" under Section 22(k) of the Internal Revenue Code and whether the separation agreement was indeed "incident to divorce." The court held that the 1929 agreement was incident to divorce and that the lump-sum payment of arrearages retained its character as periodic payments. Therefore, the payment was taxable income to Grant and deductible by Ross, resolving the Commissioner's inconsistent determinations.

Facts

In April 1929, Harold W. Ross and Jane C. Grant entered into a separation agreement. This agreement stipulated that Ross would transfer certain securities to Grant. If the dividends from these securities fell below $10,000 in any year, Ross was obligated to pay Grant the difference. Approximately 35 days after signing the separation agreement, divorce proceedings commenced, although the divorce decree itself did not mention alimony or the separation agreement. In 1946, Grant and Ross, both having remarried, entered into a new agreement to terminate future alimony obligations. However, this 1946 agreement explicitly stated that Ross remained liable for any alimony arrearages accumulated up to January 1, 1946. Ross then paid Grant a lump sum of $10,720, which was determined to be the exact amount of alimony arrearages owed under the 1929 agreement.

Procedural History

The Commissioner of Internal Revenue determined that the $10,720 received by Grant was taxable income under Section 22(k) of the Internal Revenue Code. Simultaneously, the Commissioner determined that Ross could not deduct this $10,720 payment under Section 23(u) of the Code. The Commissioner conceded that these determinations were contradictory and could not both be correct. Grant and the Estate of Harold W. Ross (Boss) each petitioned the Tax Court to contest these determinations.

Issue(s)

1. Whether the separation agreement executed in April 1929 was "incident to" the subsequent divorce, even though the divorce decree was silent on the matter of

alimony and the agreement.

2. Whether the lump-sum payment of $10,720 in 1946, representing accumulated alimony arrearages, constituted “periodic payments” within the meaning of Section 22(k) of the Internal Revenue Code.

Holding

1. Yes, because the separation agreement was followed by a divorce action within a short period (35 days), indicating it was made in contemplation of divorce and thus incident to it.

2. Yes, because the lump-sum payment represented the aggregate of previously accrued periodic alimony payments. Arrearages retain their original character as periodic payments even when paid in a lump sum.

Court’s Reasoning

Regarding whether the separation agreement was incident to divorce, the court emphasized that an agreement can be incident to divorce even if not explicitly mentioned in the divorce decree. The court noted that a mutually coexistent intent for divorce at the time of the agreement is not strictly required. Citing *Izrastzoff v. Commissioner*, the court stated that legislative history stresses the fairness of taxing the wife and allowing the husband a deduction for payments “in the nature of or in lieu of alimony or an allowance for support.” The court found that the close proximity between the separation agreement and the divorce proceedings sufficiently demonstrated that the agreement was incident to the divorce.

On the issue of “periodic payments,” the court reasoned that the original payments under the 1929 separation agreement were clearly periodic, as Ross was obligated to supplement dividend income to ensure Grant received at least $10,000 annually. Referencing *Mahana v. United States*, the court affirmed that such payments to make up deficits in annual yields are considered periodic. The court then addressed whether the lump-sum payment of arrearages retained this periodic nature. Relying on *Elsie B. Gale* and *Estate of Sarah L. Narischkine*, the court held that arrearages do retain their original character. Quoting *Estate of Sarah L. Narischkine*, the court stated: “Since the arrears here would have constituted periodic payments had they been paid when due, the receipt of such arrears, even though in a lump or aggregate sum, must be regarded as the receipt of a periodic payment.” Therefore, the $10,720 lump-sum payment was deemed a “periodic payment” under Section 22(k).

Practical Implications

Grant v. Commissioner provides crucial clarification on the tax treatment of alimony arrearages paid in a lump sum. It establishes that such lump-sum payments are not considered a principal sum payment but retain the character of the underlying periodic alimony payments. This means they are taxable as income to the recipient under Section 22(k) and deductible by the payor under Section 23(u). This case is important for legal practitioners in divorce and tax law, as it dictates how to structure settlements involving alimony arrearages to ensure proper tax treatment. It reinforces the principle that the original nature of the alimony obligation, rather than the form of payment, governs its taxability. Later cases have consistently followed this precedent, affirming that lump-sum payments of alimony arrearages are treated as periodic payments for federal income tax purposes, thus providing a clear rule for tax planning in divorce settlements involving outstanding alimony obligations.

