

## ***Capodanno v. Commissioner, 66 T. C. 659 (1976)***

Retroactive support payments are treated as periodic payments for tax purposes if they arise from the same marital obligation as prospective payments.

### **Summary**

In *Capodanno v. Commissioner*, the Tax Court determined the tax implications of payments made by R. T. Capodanno to his separated wife, Lilley Capodanno, pursuant to a New Jersey Supreme Court decree. The court ruled that both prospective and retroactive support payments were periodic and thus taxable to Lilley and deductible by R. T. under IRC sections 71 and 215. However, a restitution payment for overpaid taxes was not considered a support payment and thus not taxable to Lilley nor deductible by R. T. The court also clarified that a separate maintenance decree does not constitute a legal separation under New Jersey law, impacting the petitioners' filing status.

### **Facts**

R. T. Capodanno and Lilley Capodanno separated in 1964. Lilley sought support through a separate maintenance action in New Jersey, which initially failed but was later awarded on appeal. The New Jersey Supreme Court ordered R. T. to pay \$400 monthly support retroactive to 1965 and awarded Lilley \$1,125 plus interest for overpaid taxes under a prior agreement. In 1971, R. T. paid Lilley \$24,990. 55, including the retroactive and prospective support, the tax restitution, and interest. Both filed separate tax returns as unmarried individuals, claiming deductions and exclusions related to these payments.

### **Procedural History**

Lilley initially filed for separate maintenance in 1965, which was denied by the trial court in 1969. The Appellate Division affirmed in 1970 with modifications, but the New Jersey Supreme Court reversed in part in 1971, awarding support. The Tax Court then considered the tax implications of these payments in 1976.

### **Issue(s)**

1. Whether the \$400 monthly payments, both retroactive and prospective, are includable in Lilley's gross income under IRC sections 71(a) and 61(a)(4) and deductible by R. T. under sections 215 and 163(a).
2. Whether the \$1,125 restitution payment for overpaid taxes is includable in Lilley's gross income and deductible by R. T.
3. Whether petitioners are legally separated under New Jersey law to file as "unmarried individuals" under IRC section 1(c).

### **Holding**

1. Yes, because the \$400 monthly payments, including the retroactive portion, were periodic payments for support, taxable to Lilley and deductible by R. T.
2. No, because the \$1,125 payment was a restitution of overpaid taxes, not a support payment, thus not taxable to Lilley nor deductible by R. T.
3. No, because a separate maintenance decree under New Jersey law does not constitute a legal separation, so petitioners cannot file as unmarried individuals.

### **Court's Reasoning**

The court distinguished between periodic support payments and lump-sum payments, citing *Gale v. Commissioner* to argue that retroactive support payments are periodic if they stem from the same marital obligation as prospective payments. The court emphasized that the New Jersey Supreme Court's decision considered Lilley's "needs" in determining the support amount, aligning with the tax code's definition of periodic payments. The \$1,125 restitution payment was treated separately as it arose from a contractual obligation, not marital support. Regarding legal separation, the court relied on *Boettiger v. Commissioner* and *Weinkrantz v. Weinkrantz*, stating that a separate maintenance decree in New Jersey does not alter the marital relationship enough to qualify as a legal separation. The court also found Lilley negligent for not reporting the interest income, applying a negligence penalty under IRC section 6653(a).

### **Practical Implications**

This decision clarifies that retroactive support payments can be treated as periodic for tax purposes, affecting how attorneys should advise clients in similar situations. It also underscores the importance of distinguishing between payments arising from marital obligations and those from separate contractual agreements. The ruling on legal separation under New Jersey law impacts how separated couples file their taxes and may influence similar cases in states with comparable statutes. Practitioners should be aware of the potential for negligence penalties when clients fail to report income from support-related payments accurately. Subsequent cases have cited *Capodanno* in analyzing the tax treatment of support payments and the definition of legal separation.