

MARGARET A. KELLEY
1384 Jug Factory Road
Wetumpka, AL 36092,

Taxpayer,

v.

STATE OF ALABAMA
DEPARTMENT OF REVENUE.

STATE OF ALABAMA
DEPARTMENT OF REVENUE
ADMINISTRATIVE LAW DIVISION

DOCKET NO. INC. 97-269

FINAL ORDER

The Revenue Department assessed income tax against Margaret A. Kelley ("Taxpayer") for the years 1991 - 1995. The Taxpayer appealed to the Administrative Law Division, and a hearing was conducted on September 9, 1997. Alan Taunton and Tom Sullivan represented the Taxpayer. Assistant Counsel Margaret McNeill represented the Department. The Taxpayer's ex-husband, Charles D. Kelley, intervened in the case, but failed to appear at the hearing.

The issue is whether certain payments received by the Taxpayer from her ex-husband pursuant to a 1991 divorce decree constituted "alimony and separate maintenance payments" pursuant to Code of Ala. 1975, 40-18-14(1). If so, the payments must be included as gross income by the Taxpayer, and can be deducted by the ex-husband.

The Taxpayer divorced in 1991. The divorce decree requires the ex-husband to pay the Taxpayer 40 percent of his net bi-weekly salary received from the Alabama Department of Conservation. After retirement, the ex-husband is required to pay the Taxpayer 40 percent of his net retirement pay. The decree does not address whether the payments stop if the Taxpayer dies before her ex-husband.

The Taxpayer failed to report the payments as gross income on her Alabama income tax returns for the subject years. The Department audited the Taxpayer, included the payments in the Taxpayer's gross income, and accordingly entered the final assessments in issue.

Alimony must be reported as gross income by the payee spouse, and can be deducted by the payor spouse. "Alimony" is defined for Alabama purposes the same as for federal purposes at 26 U.S.C. 71. Code of Ala. 1975, 40-18-14(1).

Before 1984, the 71 definition of "alimony" for tax purposes was complex and uncertain. See Taxpayer's brief at page six. However, Congress simplified the definition by amending 71 in 1984 and 1986. Under current ("post-1984") law, payments qualify as alimony pursuant to 71(b)(1) if four conditions are met;

"(A) such payment is received by (or on behalf of) a spouse under a divorce or separation agreement,

(B) the divorce or separation instrument does not designate such payment as a payment which is not includible in gross income under this section and not allowable as a deduction under section 215,

(C) in the case of an individual legally separated from his spouse under a decree of divorce or separate maintenance, the payee spouse and the payor spouse are not members of the same household at the time such payment is made, and

(D) there is no liability to make any such payment for any period after the death of the payee spouse and there is no liability to make any payment (in cash or property) as a substitute for such payment after the death of the payee spouse."

This case turns on paragraph (D) above. The Department argues that because the divorce decree is silent as to whether the payments stop if the Taxpayer dies, the payments qualify as alimony under paragraph (D), citing Department Reg. 810-3-14-

.01(10)(c)3. That regulation specifies that the decree need not expressly state that the payments will cease on the payee spouse's death.

I agree with the Department regulation that the decree no longer has to specify that payments will stop on the payee spouse's death. I disagree, however, with the Department's assumption that if the decree is silent on the issue, the payments automatically qualify as alimony under paragraph (D).

Before 1984, payments qualified as alimony only if the divorce decree specified that the payments would cease when the payee spouse died. If the decree was silent, the payments were not alimony. See, Temporary IRC Reg. 1.71-1T(Q/A 11&12), cited in the Taxpayer's brief at page four.

However, the above IRC regulation does not reflect the 1984 and 1986 amendments to 71. See, CCH Standard Federal Tax Reporter, 1997, Vol. 1, Para. 6092.

Under post-1984 law, the decree no longer has to expressly provide for termination for the payments to qualify as alimony. The above CCH source, at Para. 6094.02, explains:

"Under the post-1984 rules, payments must meet all of the following requirements in order to be considered alimony, to be deductible by the payor and to be includible in the income of the payee spouse;

* * *

5. Payments must terminate at the death of the payee spouse and there must be no liability to make any payment (in cash or property) as a substitute for such payment. It is sufficient if the payments terminate by operation of the relevant state law. The divorce or separate instrument does not need to expressly provide for termination."

Consequently, Department Reg. 810-3-14-.01(10)(c)3 is correct that the decree need not expressly state that the payments will terminate on the payee spouse's death.

However, the Department incorrectly assumes that if the decree is silent on the issue, the

payments qualify as alimony. Rather, if the decree is silent, as in this case, the issue turns on whether the payor spouse is still obligated to make the payments after the death of the payee spouse under operation of state law. Consequently, the deciding question in this case is whether the ex-husband would be obligated under Alabama law to continue paying the Taxpayer's estate in the event of her death.

The divorce decree provides that the ex-husband shall pay 40 percent of his net salary to the Taxpayer, and then 40 percent of his retirement pay after he retires. If the Taxpayer dies before her ex-husband, I can find no reason under Alabama law why the ex-husband would not still be legally obligated to pay her estate under the divorce decree. Because the payments would not cease upon the Taxpayer's death, they do not qualify as alimony under 71(b)(1)(D). Consequently, the payments are not taxable to the Taxpayer. For authority supporting the above conclusion, see M. Stokes, 68 TCM 705, TC Memo. 1994-456; IRS Letter Ruling 9542001, July 10, 1995; see generally, CCH Standard Federal Tax Reporter, 1997 Vol. 1, Para. 6094.38.

The final assessments in issue are dismissed. This Final Order may be appealed to circuit court within 30 days pursuant to Code of Alabama 1975, 40-2A-9(g).

Entered October 1, 1997.

BILL THOMPSON
Chief Administrative Law Judge

BT:ks

cc: Margaret McNeill, Esq.
J. Alan Taunton, CPA
Tom Sullivan, Esq.
Charles D. Kelley
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