No. 11686.

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

Estate of Homer Laughlin,

Deceased,

Beach D. Lyon, Administrator with the will annexed,

Petitioner,

vs.

Commissioner of Internal Revenue,

Respondent.

PETITIONER'S OPENING BRIEF.

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Opinion Below.

The opinion of the Tax Court is reported in 8 T. C. 33. A copy is printed in the Record, at pages 90 to 116.

Jurisdiction.

This petition for review [R. 120-123] involves an asserted deficiency in income taxes for the taxable year 1942. The notice of deficiency is dated June 6, 1944 [R. 12]. The taxpayer's petition for redetermination was filed with the Tax Court of the United States August 25, 1944 [R. 20] under the provisions of Section 272 of the Internal Revenue Code. The decision of the Tax

Court determining that there was a deficiency in income tax for the year 1942 in the amount of $7,747.89 was entered on March 26, 1947 [R. 119]. The case is brought to this Court by a petition for review filed by the taxpayer on June 20, 1947 [R. 126], pursuant to the provisions of Sections 1141 and 1142 of the Internal Revenue Code, the return of the tax in respect of which the claimed liability arises having been made to the Collector's office for the Sixth District of California [R. 4].

Question Presented.

Taxpayer, during the year 1942, paid $9,600.00 to Ada Edwards Laughlin, divorced wife of the decedent Homer Laughlin, pursuant to a contract entered into between decedent and Ada Edwards Laughlin, incident to the divorce, providing for payment to Ada Edwards Laughlin of $800.00 per month for her life, in discharge of the decedent's legal obligation of support. The decedent's estate, the present petitioner, contends that the $9,600.00 payment is deductible from the estate's income (Sections 22(k), 23(u), 171(b), Internal Revenue Code). The denial of this deduction by the Commissioner and the Tax Court is the occasion of this petition for review.

Statutes Involved.

The statutes involved are Sections 22(k), 23(u), 162(b), 162(d), 171(a), and 171(b), Internal Revenue Code. These statutes, or the parts thereof deemed necessary for the decision of this case, are set out in the appendix.

Statement of the Case.

On April 1, 1924, Homer Laughlin (sometimes referred to as Homer Laughlin, Jr.), and his then wife, Ada Edwards Laughlin, entered into a property settlement agreement [Ex. F; R. 53]. An action for divorce was instituted in the Superior Court, Los Angeles County, by Ada E. Laughlin shortly thereafter against Homer Laughlin, an interlocutory decree being entered on September 24, 1924, followed by final decree, September 29, 1925. The decrees [Ex. G; R. 67] approve and confirm the property settlement agreement, the final decree setting it forth in *haec verba* [R. 68].

The $800.00 per month agreed to be paid by Homer Laughlin to Ada E. Laughlin during her life (to be reduced to $300.00 per month if she remarried—an event which has never happened) were made, as the agreement [Ex. F, par. 1; R. 53] shows, for her support and maintenance. It was stipulated that Homer Laughlin, Jr., had no substantial amount of community property at the time of the April 1, 1924, agreement, or at any time thereafter during the continuance of the marriage between him and Ada Edwards Laughlin, his holdings consisting of property given to him by or inherited by him from his father, Homer Laughlin, Sr.[1]

The stipulated payments to Mrs. Laughlin were expressly made an obligation of Homer Laughlin's estate [Ex. F, par. 10; R. 65]. The $9,600.00 payment made

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[1]The above statement is made in view of the fact that the property settlement agreement [Ex. F, pars. 6 and 7; R. 58, 59] contains customary recitals whereby each party released any interest in the property of the other and the wife released any interest in the community property.

during the year in question, 1942, was made by petitioner pursuant to the agreement of April 1, 1924, and the divorce decrees [R. 36].

Homer Laughlin died on December 27, 1932 [R. 32]. Beach D. Lyon is, and during the year 1942 was, administrator with will annexed of his estate [R. 4, 12].

Further facts relating to an alleged deduction of the Ada E. Laughlin claim for estate tax purposes in the estate of Homer Laughlin, deceased, will be referred to in an appropriate connection (see p. 16, *infra*).

Specification of Errors.

Petitioner respectfully submits that the Tax Court erred,

1. In holding and deciding that the sum of $9,600.00 paid by the petitioner to Ada Edwards Laughlin during the taxable year 1942 was not deductible for federal income tax purposes from the income of the petitioner for that year.

2. In holding and deciding that there was any deficiency in any sum whatever in the payment of the petitioner's federal income tax for the taxable year 1942.

3. In rendering an opinion and decision which, in the respects above enumerated, are contrary to the law and the regulations, and not supported by the evidence in the case.

Summary of Argument.

Section 22(k), Internal Revenue Code, provides for including in the income of a divorced wife, periodic payments made in discharge of a legal obligation arising out of the marital relationship which is imposed upon the husband by the divorce decree or a written instrument incidental thereto. The coordinate provisions of Section 23(u) allow a deduction to the husband, of such payments. Section 22(k) in the concluding sentence refers to Section 171(b) for the rule governing cases "where such periodic payments are attributable *to property of an estate* or property held in trust" (emphasis supplied). Section 171(b) expressly states that "for the purposes of computing *the net income of the estate* or trust and the net income of the wife," the latter "shall be considered as the beneficiary specified in this supplement"—that is, payments to her are deductible under Section 162(b), being given the tax status of "income * * * which is to be distributed currently by the fiduciary to the legatees, heirs or beneficiaries" (Sec. 162(b)).

Argument.

We shall discuss the case under two main headings, namely

I. Effect of Sections 22(k), 171(b) and Related Sections.

II. Effect of Certain Proceedings Had in Determining the Estate Tax on Homer Laughlin's Estate.

Taking up these points in order:

I.

Effect of Section 22 (k), 171 (b) and Related Sections.

Preliminarily, it is clear that if Homer Laughlin were living he would be entitled to the benefits of Section 23(u), allowing a deduction to the husband for amounts includible in the wife's income under Section 22(k). We have here a case of a wife "who is divorced * * * from her husband under a decree of divorce." (Sec. 22(k).) The payments are made "in discharge of * * * a legal obligation which, because of the marital or family relationship, is imposed upon or incurred by such husband under such decree or under a written instrument incident to such divorce."

Except in one respect which will be noted below, the payments come within the strictest interpretation of the Commissioner's own regulations. See Regs. 111, Sec. 29.22(k)-1(a), *infra*, p. 9. No part of the payments is attributable to "any interest in property transferred in discharge of the husband's obligation under the decree or instrument incident thereto, which interest originally belonged to the wife." (Reg. Sec. 29.22(k)-1(b).)

It is agreed [R. 38] that Homer Laughlin, Jr., did not possess at the time of the settlement agreement of April 1, 1924 [Ex. F; R. 53] or at any time thereafter during the subsequent brief period of his marriage to Ada Edwards Laughlin, any substantial amount of community property.

The question of property rights does not enter into this controversy, the sums in question being payable, as paragraph 1 of the contract provides, "for the support and maintenance" of the wife. Apropos of a similar contract, the Tax Court has said, in *Lewis Cass Ledyard,* C. C. H. Dec. 15,087(M), T.C., Mar. 20, 1946 (app. dism., C. C. A. 2):

> "* * * The fact that the Fourth Paragraph contains mutual releases of dower and other property rights does not justify the conversion of a part of a fund provided for maintenance and support into a payment for release of such rights. The mutual releases have no apparent connection with the settlement of the wife's rights to maintenance and of the obligation of petitioner to support his minor child."

The payments of $800.00 per month made during 1942 would clearly have been deductible by Homer Laughlin (Int. Rev. Code, Sec. 23(u)) and included in Ada's income (Sec. 22(k)), if Homer had been alive during 1942.

What is the effect of Homer Laughlin's death? Is his estate, now the payor, entitled to deduct these payments?

The answer is, Yes, if Ada Laughlin is a "beneficiary" as that term is used in Supp. E (Estates and Trusts), Sections 161-172, Internal Revenue Code.

Section 171(b), Internal Revenue Code, provides:

> "WIFE CONSIDERED A BENEFICIARY.—For the purposes of computing the net income of the *estate* or trust and the net income of the *wife* described in section 22(k) or subsection (a) of this section, such *wife* shall be considered as the beneficiary specified in this supplement. A periodic payment under section 22(k) to any part of which the provisions of this supplement are applicable shall be included in the gross income of the beneficiary in the taxable year in which under this supplement such part is required to be included." (Emphasis supplied.)

Now a Section 22(k) "wife" is, *inter alia,* by definition, an ex-wife "divorced * * * from her husband," receiving periodic payments "in discharge of * * * a legal obligation which * * * is imposed upon or incurred by such husband under such decree or under a written instrument incident to such divorce * * *."

Ada Laughlin qualifies under that definition. She is "divorced from" her husband. She is receiving "periodic payments." These are made "in discharge of" the husband's legal obligation under the decree. Ada Laughlin is therefore a "wife described in section 22(k)" (Sec. 171(b)). Being such a wife, she is "the beneficiary specified" in Supp. E, of which Section 171(b) is a part. Being such beneficiary, she is chargeable with the tax on such "income." As a necessary consequence, the payments are deductible by the estate under Section 162(b).

Section 171(b), we submit, is susceptible of no other construction. Had it referred only to *trusts*, the rule might be different. But the rule that the "wife" is the "beneficiary" applies both to estates and trusts. The term *estate* has no meaning unless it is construed as referring to the estate of a deceased husband who was subject to the liabilities (of support and maintenance) imposed upon him by divorce decree or by agreement incident thereto. The term *wife* is not an abstraction. It connotes husband. The use of the word *estate* contemplates that the husband's estate, a legal entity and the continuation of his legal personality, succeeds him for the purposes of the statute. Succeeding him and bearing his burdens, it stands in his shoes, is entitled to his deductions.

What is inequitable or even strange in this result? Congress could hardly have made its intent clearer, although it might have chosen words more carefully than to speak of the *beneficiary* of an *estate.* But the context must be considered. Congress in Section 171(b) is speaking of the "income of the estate or trust." Obviously, it would not do to speak of a divorced wife receiving alimony as a legatee or heir (Sec. 162(b), (c)). It was thought sufficient to say that such a wife "shall be considered" as a beneficiary, even of an estate (171(b)). There seems to be no objection to *considering* her in that light; that is, awarding her the benefits and subjecting her to the burdens which result from the status of being the *beneficiary* of an *estate,* to the extent, and with the effect, specified in the statute.

Section 29.22(k)-1(a) of Reg. 111 is in harmony with the above. It provides (in part):

> "Periodic payments are includible in the wife's income under section 22(k) only for the taxable year in which received by her. As to such amounts, the wife is to be treated as if she makes her income tax returns on the cash receipts and disbursements basis, regardless of whether she normally makes such re-

> turns on the accrual basis. However, if the periodic payments described in section 22(k) *are to be made by an estate* or trust, such periodic payments are to be included in the wife's taxable year in which they are includible according to the rules as to income of estates and trusts provided in sections 162, 164 and 171(b), *whether or not such payments are made out of the income of such estates or trusts.*" (Emphasis supplied.)

To be compared with the foregoing is the following from Reg. 111, Section 29.23(u)-1 (in part):

> "The deduction under section 23(u) is allowed only to the obligor spouse. It is not allowed to an estate, trust, corporation, or any other person who may pay the alimony obligation of such obligor spouse. * * *"

Reg. 111, Section 29.171-2, applicable to Internal Revenue Code, Section 171(b), does not deal with—it ignores —payments by estates.

Possibly the apparent conflict between Sections 29.22(k)-1(a) and 29.23(u)-1 of the regulations can be reconciled. It may be that in 29.23(u)-1, in speaking of an estate, trust, etc., as not being entitled to the deduction, the Treasury did not think it necessary to except the plain case *where the estate of the deceased husband* makes the payments. The Treasury may not have thought it necessary to deny that it was withholding a privilege which the statute expressly grants. As a responsible agency of the government, it may have assumed that no one would attribute to it an intent to nullify an act of Congress.

We think the Treasury is entitled to the benefit of the construction above suggested. If we are wrong in this, if Section 29.23(u)-1 does say that the estate of a *deceased husband,* obligated to make the payments, is not entitled to the deduction, we believe it to be in conflict not only with the coordinate regulation, Section 29.22(k)-1(a), but with Section 171(b), Internal Revenue Code. The latter obviously must prevail over all inconsistent regulations and rulings. (*Manhattan General Equipment Co. v. Commissioner,* 297 U. S. 129, 80 L. Ed. 528, 56 S. Ct. 397; *Koshland v. Helvering,* 298 U. S. 441, 80 L. Ed. 1268, 56 S. Ct. 767.) It requires, we submit, the the taxpayer be allowed as a deduction the $9,600.00 paid to Ada Edwards Laughlin in 1942.

We shall now refer to the reasons advanced by the learned Tax Court for upholding the claimed deficiency.

Petitioner's argument on this point in the Tax Court is summarized at pages 43 and 44 of 8 T. C. The Tax Court's answer to this argument is dependent entirely on the proposition that the Laughlin agreement did not require that the $9,600.00 be paid out of income.

We agree as to the fact, but not as to its consequences. The Tax Court's holding overlooks, we submit, the effect of Section 162(d), Internal Revenue Code, added in 1942. That section provides, in part:

> "In cases where the amount paid, credited, or to be distributed can be paid, credited, or distributed out of other than income, the amount paid, credited, or to be distributed (except under a gift, bequest, devise, or inheritance not to be paid, credited, or dis-

tributed at intervals) during the taxable year of the estate or trust shall be considered as income of the estate or trust which is paid, credited, or to be distributed if the aggregate of such amounts so paid, credited, or to be distributed does not exceed the distributable income of the estate or trust for its taxable year. * * *"

In support of its conclusion, the Tax Court quotes [p. 44 of 8 T. C.; R. 111] from the report of the Senate Finance Committee (1942-2 C. B. 569) which accompanied the revenue bill later enacted into law. Following is the whole of the paragraph in question, including the opening sentence, not quoted in the Tax Court's opinion:

"The general rules for accounting for the income of a trust *or estate*, prescribed in Supplement E of Chapter 1, apply to that part of any periodic payment which is a distribution of income of the trust *or estate* and which is required under section 22(k) or section 171(a) to be included in the income of the individual receiving such payment. For the purpose of clarity, this section provides that the wife entitled to receive the payment is considered as the beneficiary of the trust. If these provisions of section 171(b) apply to any part of a periodic payment required under section 22(k) to be included in income of the beneficiary, the whole of such periodic payment shall be included in gross income of the beneficiary in the taxable year in which under the above provisions of section 171(b) such part is required to be included in her income. It is contemplated under these pro-

> visions that the trust *or estate will be entitled to a deduction* in computing its net income for amounts required to be included in the wife's income under section 22(k) or section 171 *to the extent that such amounts are paid, credited, or to be distributed out of income of the estate* or trust for its taxable year." (Emphasis supplied.)

The effect of this, we submit, is the exact opposite of the inference which the Tax Court draws from it. The Senate Finance Committee was referring to the new concept introduced into the law by the Revenue Act of 1942, whereby a beneficiary entitled to benefits not limited to income becomes, for the first time, conclusively regarded as a recipient of, and taxable upon, income to the extent that the stipulated payments do not exceed the distributable income of the estate or trust (Sec. 162(d), Int. Rev. Code, quoted above, page 11), overruling *Helvering v. Pardee,* 290 U. S. 365, 78 L. Ed. 365, 54 S. Ct. 221; and *Burnet v. Whitehouse,* 283 U. S. 148, 75 L. Ed. 916, 51 S. Ct. 374.

The Senate Committee report shows that the Committee recognized the effect of its handiwork in the respect now under consideration. In the opening sentence of the excerpt quoted above, the Committee gives express recognition to the fact that Supplement E to Chapter 1 (Secs. 161-173, Int. Rev. Code) applies not only to trusts but to estates. The "beneficiary" of an estate as well as of a trust is required to pay the tax on the income. An "estate" as well as a trust is entitled to the deduction.

The Tax Court's opinion, in the respect now under consideration, is contrary to Regulations 111, Section 29.22(k)-1(a), quoted above, page 9. In that section of the Regulations the Commissioner correctly says that periodic payments are to be included in the wife's income "whether or not such payments are made out of the income of such *estates or* trusts."

In the case at bar the income of the estate was abundantly ample to permit the $9,600.00 to be paid out of income. As the record shows, the net income of the estate for 1942 as adjusted by respondent, was $67,203.18 [R. 16]—slightly more than seven times the amount required to be paid Mrs. Laughlin. This, we submit, brings the case squarely within the coordinate 1942 amendments to Section 162(b) and 171(b), giving the payments the exact status they would have had if required to be paid out of income, and making applicable the following excerpt from the Tax Court's opinion, page 45 of 8 T. C.:

> "As we have already indicated, if decedent's divorced wife, Ada, had been one to whom income was currently distributable by the estate, then it is reasonable to believe that she would be a 'beneficiary' of the estate as provided by section 171(b), upon which petitioner relies."

We feel that we should not detain the Court with a discussion of academic problems. If we had no income, we should not need the deduction, in fact, we would not be here. The right to the deduction under such circumstances, existing only *in vacuo,* would have only a speculative interest. We are willing to accept the limitation suggested by the Tax Court, that the deduction applies only to the extent that Ada Laughlin can be paid out of income (Sec. 162(d), Int. Rev. Code). The recognition of this principle in no way affects the result.

It is proper to say that petitioner had no means of anticipating, and no opportunity to meet, the specific arguments on which the Tax Court relies in denying the deduction. As the Tax Court says [p. 44 of 8 T. C.; R. 110], respondent did not argue the meaning of Section 171(b) in that Court. Respondent's typewritten brief in the Tax Court disposed of this particular deduction in less than a page and a half, contending only that the deduction was barred because "in practical effect, the estate has been allowed a substantial deduction for estate tax purposes."[2]

Respondent being silent on the principal question herein involved, the Tax Court was compelled to dispose of the matter without such assistance as petitioner might otherwise have been able to give on reply. This may account for the failure, as we see it, of the Tax Court to give full effect to the implications of the coordinated legislative program (Secs. 22(k), 23(u), 162(d), 171(b)) on which we rely here.

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[2]Among "Statutes and Regulations Involved," respondent quoted, without comment, Secs. 22(k), 23(u), 162(b), 171(a) and (b), and 812(b)(3), Internal Revenue Code; also Regs. 111, Secs. 29.162-1 and 29.22(k)-1.

II.

Effect of Certain Proceedings Had in Determining the Estate Tax on Homer Laughlin's Estate.

The following are the facts regarding this matter. In Homer Laughlin's estate tax return, a deduction of $152,480.00 was claimed on account of the Ada Edwards Laughlin indebtedness, which respondent reduced to $101,-259.35 [R. 36]. Certain items of expense of administration having been omitted, petitioner filed a claim for refund [R. 37], the correctness of which respondent admitted by making an adjustment [R. 37], but nevertheless rejected the claim on the alleged ground that the $101,259.35 liability on the Ada Edwards Laughlin contract had been erroneously deducted in determining the estate tax liability. No further action was taken by either party regarding these matters [R. 37].

The allowance to the estate of Homer Laughlin, Jr., of a deduction on account of the Ada Edwards Laughlin claim was at least partially nullified by the Commissioner's later action in denying the estate an admittedly proper refund. The net advantage to the estate of the Commissioner's mistake, if it was a mistake, in permitting the deduction of the Ada Edwards Laughlin claim was therefore materially reduced.

The present case stands, we submit, on its own merits, unaffected by past errors. All that is water over the dam. We may concede the general correctness of respondent's statement, quoted by the Tax Court (p. 43 of 8 T. C.), that "Ordinarily the payment of a debt of a decedent by his estate does not furnish a foundation for an income tax deduction." Paraphrasing this statement, in fact going somewhat further, we may say that "Ordinarily the payment of a debt * * * does not furnish the foundation of an income tax deduction" to anyone. We do not "found" any claim to an income tax deduction on the ground that the Commissioner erroneously failed to give us the full benefit of an estate tax deduction. Our case is not predicated on the Commissioner's past errors in unrelated, or only remotely related, matters. Nor can the Commissioner prevail here because the estate obtained a part of the estate tax deduction to which it was entitled on account of Mrs. Laughlin's claim. He could not prevail if the estate had obtained that benefit *in toto*. It cannot be too strongly emphasized that here we are dealing with no ordinary situation. Section 22(k) "income" is income, even though paid out of principal (Reg. 111, Sec. 29.22(k)-1 pars. (a) and (b)). The "husband," when he makes such payments during his lifetime, *is discharging a debt.* But he is entitled to a deduction for the payments because the statute so provides.

How is the deceased husband's estate, under a continuing liability for the payments, in any different situation? The obligation, being a debt, is deductible for estate tax purposes (*Estate of Maresi,* 6 T. C. 583, affd., 156 F. (2d) 929 (C. C. A. 2)). *But the obligation was a debt to the husband while living.* If, as the statute expressly says, a living husband, owing a debt, is nevertheless entitled to deduct payments made on it, there is nothing impossible or even strange in giving his estate a like deduction for payments made out of income, when the estate is subject to the identical burden.

It will not do to speak in generalities here. We are dealing with a new concept, somewhat revolutionary in theory, and have only to determine the extent of the relief (to payors on the one hand) and of the corresponding burden (to payees, on the other) which Congress intended to grant or to impose by the 1942 legislation (Secs. 22(k), 23(u), 171(b), Int. Rev. Code). The intention of Congress was to deal with this matter effectively, and in a large way, even going so far as to tax as "income" payments which are not income at all in any economic sense, and anomalously allowing a deduction to a man for paying a debt. Laying aside preconceptions based on the "ordinary" situations to which the above quoted statement of respondent seemingly refers, and viewing the 1942 legislation on this subject as a harmoniously consistent program, we believe that the consequences pointed out under our first heading follow.

It should be noted that the rule of *Dobson v. Commissioner,* 320 U. S. 489, 88 L. Ed. 248, 64 S. Ct. 239, is not applicable here. There is no question of fact involved in this case. The only question is one of law, namely, whether the statute requires the deduction of the payments here in question.

Conclusion.

We respectfully submit that the decision of the Tax Court should be reversed and the deficiency expunged.

Respectfully submitted,

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August 20, 1947.

APPENDIX.

Statutes involved.

Internal Revenue Code.

Sec. 22. Gross Income.

* * * * * * * * *

(k) (in part) Alimony, etc., Income.—In the case of a wife who is divorced or legally separated from her husband under a decree of divorce or of separate maintenance, periodic payments (whether or not made at regular intervals) received subsequent to such decree in discharge of, or attributable to property transferred (in trust or otherwise) in discharge of, a legal obligation which, because of the marital or family relationship, is imposed upon or incurred by such husband under such decree or under a written instrument incident to such divorce or separation shall be includible in the gross income of such wife, and such amounts received as are attributable to property so transferred shall not be includible in the gross income of such husband. * * *

Sec. 23. Deductions From Gross Income.

In computing net income there shall be allowed as deductions:

* * * * * * * * *

(u) Alimony, etc., Payments.—In the case of a husband described in section 22(k), amounts includible under section 22(k) in the gross income of his wife, payment of which is made within the husband's taxable year. If the amount of any such payment is, under section 22(k) or section 171, stated to be not includible in such husband's gross income, no deduction shall be allowed with respect to such payment under this subsection.

* * * * * * * * *

Sec. 162. Net Income.

The net income of the estate or trust shall be computed in the same manner and on the same basis as in the case of an individual, except that—

* * * * * * * * *

(b) There shall be allowed as an additional deduction in computing the net income of the estate or trust the amount of the income of the estate or trust for its taxable year which is to be distributed currently by the fiduciary to the legatees, heirs, or beneficiaries, but the amount so allowed as a deduction shall be included in computing the net income of the legatees, heirs, or beneficiaries whether distributed to them or not. As used in this subsection, "income which is to be distributed currently" includes income for the taxable year of the estate or trust which, within the taxable year, becomes payable to the legatee, heir, or beneficiary. Any amount allowed as a deduction under this paragraph shall not be allowed as a deduction under subsection (c) of this section in the same or any succeeding taxable year;

* * * * * * * * *

(d) Rules for Application of Subsections (B) and (C).—For the purposes of subsections (b) and (c)—

(1) (in part) Amounts Distributable Out of Income or Corpus.—In cases where the amount paid, credited, or distributed can be paid, credited, or distributed

out of other than income, the amount paid, credited, or to be distributed (except under a gift, bequest, devise, or inheritance not to be paid, credited, or distributed at intervals) during the taxable year of the estate or trust shall be considered as income of the estate or trust which is paid, credited, or to be distributed if the aggregate of such amounts so paid, credited, or to be distributed does not exceed the distributable income of the estate or trust for its taxable year.

* * * * * * * * *

SEC. 171. INCOME OF AN ESTATE OR TRUST IN CASE OF DIVORCE, ETC.

* * * * * * * * *

(a) INCLUSION IN GROSS INCOME.—There shall be included in the gross income of a wife who is divorced or legally separated under a decree of divorce or of separate maintenance the amount of the income of any trust which such wife is entitled to receive and which, except for the provisions of this section, would be includible in the gross income of her husband, and such amount shall not, despite section 166, section 167, or any other provision of this chapter, be includible in the gross income of such husband. This subsection shall not apply to that part of any such income of the trust which the terms of the decree or trust instrument fix, in terms of an amount of money or a portion of such income, as a sum which is payable for the support of minor children of such husband. In case such income is less than the amount specified in the decree or instrument, for the purpose of applying the preceding sentence, such income, to the extent of such sum payable for such support, shall be considered a payment for such support.

(b) Wife Considered a Beneficiary.—For the purposes of computing the net income of the estate or trust and the net income of the wife described in section 22(k) or subsection (a) of this section, such wife shall be considered as the beneficiary specified in this supplement. A periodic payment under section 22(k) to any part of which the provisions of this supplement are applicable shall be included in the gross income of the beneficiary in the taxable year in which under this supplement such part is required to be included.

Reg. 111, Sec. 29.22(k)-1 (in part): Alimony and Separate Maintenance Payments—Income to Former Wife.—(a) (in part) *In general.*—Section 22(k) provides rules for treatment in certain cases of payments in the nature of or in lieu of alimony or an allowance for support as between spouses who are divorced or legally separated under a court order or decree. For convenience, the payee spouse will hereafter in this section of the regulations be referred to as the "wife" and the spouse from whom she is divorced or legally separated as the "husband." See section 3797(a)(17).

In general, section 22(k) requires the inclusion in the gross income of the wife of periodic payments (whether or not made at regular intervals) received by her after the decree of divorce or of separate maintenance. Such periodic payments may be received from either of the two following sources:

(1) In discharge of a legal obligation which, because of the marital or family relationship, is imposed upon or incurred by the husband, or

(2) Attributable to property transferred (in trust or otherwise) in discharge of a legal obligation which, be-

cause of the marital or family relationship, is imposed upon or incurred by the husband.

The obligation of the husband must be imposed upon him or assumed by him (or made specific) under either of the following:

(1) A court order or decree divorcing or legally separating the husband and wife, or

(2) A written instrument incident to such divorce or legal separation.

* * * * * * * * *

Periodic payments are includible in the wife's income under section 22(k) only for the taxable year in which received by her. As to such amounts, the wife is to be treated as if she makes her income tax returns on the cash receipts and disbursements basis, regardless of whether she normally makes such returns on the accrual basis. However, if the periodic payments described in section 22(k) are to be made by an estate or trust, such periodic payments are to be included in the wife's taxable year in which they are includible according to the rules as to income of estates and trusts provided in sections 162, 164, and 171(b), whether or not such payments are made out of the income of such estates or trusts.

(b) (in part) *Alimony income attributable to property.*—The full amount of periodic payments received under the circumstances described in section 22(k) is required to be included in the gross income of the recipient whether such amounts are derived, in whole or in part, from income received or accrued by the source to which such payments are attributable. Thus, it matters not that such payments are attributable to property in trust, to life insurance, endowment, or annuity contracts, or to any other interest in property, or are paid directly or indirectly by the obligor husband from his income or capital. For example, if in order to meet an alimony obligation of $500 a month, the husband purchases or assigns for the benefit of his former wife a commercial annuity contract paying such amount, the full $500 a month received by the wife is includible in her income, and no part of such amount is includible in the husband's income or deductible by him. See sections 22(b)(2)(A) and section 29.22(b)(2)-4. Likewise, if property is transferred by the husband, subject to an annual charge of $5,000, payable to his former wife in discharge of his alimony obligation under the divorce decree, the $5,000 received annually is, under section 22(k), includible in the wife's income, regardless of whether such amount is paid out of income or principal of the property.

The same rule applies to periodic payments attributable to property in trust. The full amount of periodic payments to which section 22(k) applies is includible in the wife's income, regardless of whether such payments are made out of trust income.

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Section 22(k) does not apply to that part of any periodic payment attributable to that portion of any interest in property transferred in discharge of the husband's obligation under the decree or instrument incident thereto, which interest originally belonged to the wife. It will apply, however, if she receives such interest from her husband in contemplation of or as an incident to the divorce or separation without adequate and full consideration in money or money's worth, other than the release of the husband or his property from marital obligations. * * *