

BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

In the Matter of the Appeal of)
ALBERT D. AND BETTY J. ROBERTS)

Appearances:

For Appellants: Albert D. and Betty J. Roberts,
in pro. per.

For Respondent: Kendall Kinyon
Counsel

O P I N I O N

This appeal is made pursuant to section 18594 of the Revenue and Taxation Code from the action of the Franchise Tax Board on the protest of Albert D. and Betty J. Roberts against proposed assessments of additional personal income tax in the amounts of \$244.66, \$431.16 and \$507.81 for the years 1972, 1973 and 1974, respectively.

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The sole question for decision is whether appellants were entitled to larger alimony deductions than those allowed them by respondent for the years 1972, 1973 and 1974.

In 1969 Albert D. Roberts (hereafter referred to as Albert or appellant) and his former wife, Kathleen, were living separately. On June 11, 1969, they executed a property settlement agreement and the provisions of that agreement were subsequently approved by the superior court and incorporated into an interlocutory judgment^{1/} of dissolution of marriage issued on January 15, 1970. In due course that judgment became final and thereafter Albert married his present wife, Betty J. Roberts.

The first section of the property settlement agreement executed by Albert and Kathleen purported to "settle and adjust their property and support rights." In paragraph (1) of that section, Kathleen transferred to Albert all her right, title and interest in: (a) his clothing and personal effects; (b) a business known as Al Roberts Used Cars, Inc., dba ALCO Leasing Company and Anaheim-Ball Auto Sales; (c) a business known as Al Roberts Plymouth, Inc.; (d) a corporation known as Albert D. Roberts, Inc.; (e-h) their shares of stock in four corporations; (i) a parcel of real property on Garden Grove Boulevard in Garden Grove, California; (j) a promissory note of Albert D. Roberts, Inc., with a \$6,000 **balance due**; and (k) existing insurance policies on Albert's life.

By paragraph (2), Albert transferred to Kathleen all his right, title and interest in: (a) their family residence on Oma Place in Garden Grove, California; (b) its furniture and furnishings; and (c) her clothing and personal effects, including jewelry. The agreement also provided that Kathleen was to have custody of their two minor children and Albert was to pay a total of \$600 per

^{1/} Although the record does not reveal when Albert and Kathleen were married, we do know that six children were born of that marriage, and that as of June 11, 1969, three of those children had reached age twenty-one and a fourth child was nineteen years of age and married. These facts indicate that the marriage was of substantial duration.

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month in child support, plus reasonable medical expenses of the children.

Paragraph (2) of the property settlement agreement then provided, in pertinent part:

(g) Husband is to pay to wife toward her support the sum of \$300 per month as alimony payable on the first day of each month, to commence on the first day of the month following the date of the execution of this agreement;

(h) The alimony provided for herein shall terminate on the 62nd birthday of the wife, upon the death of either party, or at such time as husband pays off the balance of the two promissory notes referred to in Paragraph (2) (k) (b) and (2) (k) (c) ^{2/} below, or in the event that the wife should remarry. In no event shall the alimony payments terminate in less than five (5) years except by reason of death of either party.

* * *

(j) [As additional support of Kathleen and the minor children, Albert agreed to provide and maintain two automobiles for them, or to pay an additional \$150 per month in lieu of each automobile.]

(k) The husband is to pay to wife as her share of the community property the following:

(a) \$10,000 cash on execution of this agreement:

(b) A promissory note in the amount of \$50,000, bearing seven percent (7%) interest per annum, secured by a first deed of trust on the Garden Grove Boulevard

^{2/} The property settlement agreement contains no paragraph (2) (k) (c). It appears that the parties intended to refer to the paragraph designated (2) (1) in the agreement, which is the only other provision involving a promissory note.

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property above described in Paragraph FIRST

(1) (i) [the real property transferred to Albert], payable at the rate of \$500 per month or more, including interest, until paid. In any event, the entire principal and interest shall be payable in 15 years from the date of execution.

(1) ^{3/} A promissory note in the amount of \$40,000, bearing seven percent (7%) interest per annum, payable at the rate of \$500 or more per month including interest, with total principal and interest due and payable at the expiration of 15 years from date of execution, which note is to be accompanied by a life insurance policy on the life of the husband, naming the wife as beneficiary, in an amount in excess of the balance due on the note, the premiums to be paid by the husband: said note to be guaranteed by Al Roberts Plymouth, Inc.

* * *

(o) Husband is to make all the monthly payments under the existing deed of trust on the real property located [on] ... Oma Place, Garden Grove, California, described above in paragraph (2) (a) [the family residence transferred to Kathleen], until the complete balance is paid off. In the-event wife sells this real property herein described, husband will execute a non-interest bearing note in favor of wife in the amount of the then existing unpaid balance of the note secured by the trust deed, to be paid in monthly payments in the same amount as called for by the secured note.

In the interlocutory judgment of dissolution, the superior court reiterated the \$300 per month spousal support requirement.

Appellants filed joint California personal income tax returns for 1972, 1973 and 1974 in which they

^{3/} See footnote 2, supra.

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claimed alimony deductions in the amounts of \$12,059, \$12,567 and \$14,018, respectively. Those deductions were composed of the \$300 per month paid to Kathleen pursuant to the support order, the \$1,000 per month paid on the two promissory notes (less interest deducted), and the \$116.85 monthly house payments made on Kathleen's Garden Grove home (less interest deducted). Upon review of appellants' returns, respondent allowed them an annual alimony deduction of \$3,600, representing the \$300 per month specifically designated as support in the property settlement agreement and the judgment of dissolution. Respondent disallowed the remainder of the alimony deduction claimed for each year, and that action gave rise to this appeal.

Section 17263 of the Revenue and Taxation Code allows a husband to deduct payments made to his former wife under a divorce decree if those payments are **includible** in her gross income under section 17081. The latter section provides, in subdivision (a), that the divorced wife's gross income includes periodic payments received from her former husband in discharge of a legal obligation which, because of the marital or family relationship, is imposed on the husband under the decree or under a written instrument incident to the divorce. ^{4/} The scope of section 17081 is limited to periodic payments made because of the family or marital relationship in recognition of the general obligation to support which is made specific by the decree. (Cal. Admin. Code, tit. 18, reg. 17081-17083(a), subd. (2)(D).) Amounts paid to a wife by her former husband which are in satisfaction of her property rights, rather than her right to support, are capital in nature and are neither **includible** in her gross income under section 17081, nor deductible by the husband under section 17263. (See Cal. Admin. Code, tit. 18, reg. 17081-17083(a), subd. (3)(D); Ernest H. Mills, 54 T.C. 608 (1970), affd., 442 F.2d 1149 (10th Cir. 1971); Enid P. Mirsky, 56 T.C. 664 (1971).)

In general, the term "periodic payments", as it is used in section 17081 of the Revenue and Taxation Code, means payments made at intervals, although not necessarily equal intervals, which extend for an indefinite period or are subject to contingencies. (See Cal.

^{4/} Substantially identical provisions are contained in the federal income tax law. (See Int. Rev. Code of 1954, §§ 215(a) and 71(a) (1).)

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Admin. Code, tit. 18, reg. 17081-17083(a), subd. (4).) Conversely, installment payments discharging a part of an unconditional obligation to pay a principal sum of money which is specified in the decree will not be treated as periodic payments **includible** in the wife's **gross** income (Rev. & Tax. Code, § 17083, subd. (a) (1)), unless such installment payments could be made over a period longer than ten years from the date ~~of~~ ^{of} the decree. (Rev. & Tax. Code, § 17083, subd. (a) (2)).^{5/} Even installment payments qualifying as periodic under this exception to the general rule must still meet the requirement that they are in the nature of alimony or an allowance for support. (McCombs v. Commissioner, 397 F.2d 4 (10th Cir. 1968); Michael N. Lambros, 171,135 P-H Memo. T.C. (1971), affd., 459 F.2d 69 (6th Cir. 1972).)

The decisive question in the instant appeal, therefore, is whether the installment payments made by appellants on the two promissory notes and on Kathleen's home loan were in settlement of her community property rights, **as** respondent contends, or were in the nature of alimony or support payments.

In order to ascertain the true nature of the payments here in question, it is necessary to determine the intent of the parties to the property settlement agreement. (Phinney v. Mauk, 411 F.2d 1196 (5th Cir. 1969); George C. DeSmyter, 1173,090 P-H Memo. T.C. (1973).) To that end we must examine the terms of the agreement itself. Although the labels attached to the payments are not binding in this determination (Ann Hairston Ryker, 33 T.C. 924 (1960)), they are **persuasive** in the absence of evidence of a contrary intent. (See John F. Stone, 1164,140 P-H Memo. T.C. (1964); Bettye W. Hobbs, 163,006 P-H Memo. T.C. (1963).)

Both the property settlement agreement executed by Albert and Kathleen and the interlocutory judgment of dissolution contain an express provision for payments of \$300 per month to Kathleen for her support. (Paragraph (2)(g) of the agreement, **supra**; paragraph (5) of the judgment.) Those payments are subject to termination upon the occurrence of several contingent events, including Kathleen's remarriage or the death of either party. The presence of such contingencies modifying 'the **obligation** to make the payments is characteristic of alimony or support payments. (See Michael N. Lambros, **supra**, and Blanche Curtis Newbury, 46 T.C. 690 (1966).)

^{5/} See Int. Rev. Code of 1954, § 71(c).

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The provisions of the agreement concerning Albert's obligation to make payments to Kathleen on the two promissory notes (paragraphs 2(k) (b) and **2(1)**, supra) are preceded by the words: "The husband is to pay to wife as her share of the community property, the following:". Unlike the obligation to make support payments, Albert's liability upon execution of the notes was a fixed obligation to pay a principal sum of money. Neither Kathleen's remarriage nor the death of either party would terminate the obligation. Albert's liability under the two notes was not modifiable by a change in either his or Kathleen's economic status. In addition, both notes were secured, one by a deed of trust on the Garden Grove Boulevard property transferred to Albert, and the other by a life insurance policy on Albert's life, with Kathleen named as beneficiary, and by a guarantee executed by Al Robert's Plymouth, Inc. All of the above factors strongly indicate that the payments to be made to Kathleen on the two promissory notes were intended to be in consideration of her marital property rights rather than alimony. (See Ben C. Land, 61 T.C.' 675 (1974) and George C. DeSmyter, supra.)

The nature of the monthly payments which Albert was required to make on Kathleen's home loan (paragraph 2(o) of the agreement, supra) is not quite so clear. We observe, however, that the provision requiring Albert to make such payments is located at the end of paragraph 2' of the property settlement agreement, after the provisions regarding the two promissory notes and substantially removed from the express support provision. Furthermore, the obligation to pay the balance owing on that loan is unconditional and not subject to termination by any of the contingencies normally associated with support payments. In the event Kathleen sells the property at any time, Albert must execute a promissory note in her favor in the amount of the then existing unpaid balance of the note. We are of the opinion that these payments also lack the characteristics of alimony and are more in the nature of a part of the property settlement. (See Van Orman v. Commissioner, 418 F.2d 170 (7th Cir. 1969). aff'd. ¶68,267 P-H Memo. T.C. (1968) and Elbert G. Sharp, 1172,159 P-H Memo. T.C. (1972).)

Our tentative conclusion as to the nature of the payments here in question is buttressed by an examination of those provisions of the property settlement agreement effecting a division of the community property of Albert and Kathleen. Although the record contains no evidence of the values of the specific items transferred

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to each party, it appears that Albert received the lion's share of their community assets. We think it obvious that during more than twenty-one years of marriage, Kathleen had acquired a substantial community interest in all of those assets, and we believe it highly unlikely that she would have relinquished her valuable property interests without receiving adequate consideration.

(Appeal of Everett S. Shipp, Cal. St. Bd. of Equal., Oct. 7, 1952.) Furthermore, we note that Albert's share of the **community property** included several automobile sales and leasing businesses bearing his name. We assume that Albert actively managed those businesses and he therefore had a strong interest in **preserving** them. It is not unusual for a husband with greater "concern" for a particular business interest to agree to make payments to his wife in exchange for her interest, rather than to risk a division of the property. (See, e.g., John Sidney Thompson, 22 T.C. 275 (1954) and George C. DeSmyter, supra.)

Based on the above analysis, we must conclude that appellants' payments to Kathleen which were in excess of the amount specifically designated for her support constituted consideration for her community property rights. That being so, they were not deductible by appellants under section 17263 of the Revenue and Taxation Code.

Appellants allege that 'they claimed identical alimony deductions in their federal income tax returns for 1972, 1973 and 1974, the years on appeal. They contend that each of those returns was audited by the Internal Revenue Service, and those audits resulted in either the issuance of a "no change" letter or a refund of tax. Appellants express confusion as to why respondent has denied a portion of the total alimony deductions claimed, **when** the federal and California laws on this **subject** are virtually identical.

None of the fe'deral audit papers appear in the record, and we therefore do not know if 'the Internal Revenue Service specifically reviewed the amounts of appellants' claimed alimony deductions.; Even if it did, however, we believe that respondent was still empowered to make an **independent** examination of appellants' California personal income tax returns under its general statutory authority to examine such returns and to determine the correct amount of tax. (Rev. & Tax; Code, §§ 18582, 18583.)

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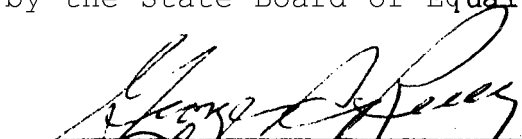
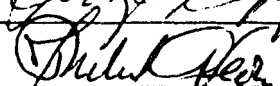

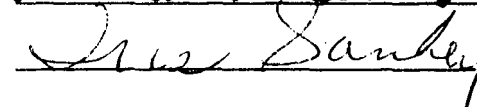
For all of the above reasons we conclude that respondent properly disallowed appellants' claimed alimony deductions in excess of \$3,600 for each year. Its action must therefore be sustained.

O R D E R

Pursuant to the views expressed in the opinion of the board on file in this proceeding, and good cause appearing therefor,

IT IS HEREBY ORDERED, ADJUDGED AND DECREED, pursuant to section 18595 of the Revenue and Taxation Code, that the action of the Franchise Tax Board on the protest of Albert D. and Betty J. Roberts against proposed assessments of additional personal income tax in **the amounts** of \$244.66, \$431.16 and \$507.81 for the years **1972, 1973** and 1974, respectively, be and the same is hereby sustained.

Done at Sacramento, California, this **26th** day of **July**, 1978, by the State Board of Equalization.


_____, Chairman

_____, Member

_____, Member

_____, Member
_____, Member