



ALIMONY TAX CHANGES UNDER THE TCJA

While many are happy about the expected increase in their take-home pay as a benefit from the Tax Cuts & Jobs Act (TCJA), few will be excited about the expected acceleration in divorces caused by a change in the treatment of alimony under the TCJA. Prior to its passage, the recipient of alimony payments was required to pick up the payments as income on their individual tax return. This allowed the payer to receive a deduction for the amount paid, which in turn, reduced the amount of taxes owed by the payer.

Under the TCJA, any divorce settlements or prenuptial agreements dated after December 31, 2018, will prevent the payer taking a deduction for alimony paid. Consequently, the recipient will no longer be required to pick up the alimony as income. This will greatly increase the net cost of providing alimony to the payer. Due to this change in net cost, we expect to see harsher negotiations in the future of divorce proceedings.

To illustrate—if a spouse is required to pay \$10,000 a month in alimony under the current regulations and is in the 50% tax bracket, including state and local taxes, and the spouse receiving the alimony is in the 30% tax bracket; a payment of \$10,000 per month would result in a net payment of \$5,000 (\$10,000 – tax deduction) for the paying spouse. The receiving spouse, at a 30% tax rate would only owe \$3,000 of tax on the receipt of the alimony. Since the spouse providing the alimony is paying a net amount of \$5,000 and the spouse receiving is getting a net payment of \$7,000, the government is supporting the spouse receiving the alimony to the extent of \$2,000 per month.

Under the future regulations, the paying spouse would experience a net cost of \$10,000 a month for providing alimony and the receiving spouse would recognize the \$10,000 alimony payment tax-free. Since the payer will no longer be able to claim the deduction, they will have more bargaining power to pay the recipient less.

With the new legislation going into effect next year, we expect to see a rush to have divorce proceedings finalized this year.