



What to do with Bonuses, Commissions, and other Variable Income

BY ERIC SCHULMAN*

Over the years, it has become common practice to build into marital settlement agreements provisions for “automatic” adjustments to child support and maintenance where the payor has variable income due to commissions, bonuses, overtime, and the like. Negotiating and inserting such provisions into the agreement served as a proactive measure to help avoid future litigation and provide a sense of fairness to both parties. Including such terms was fairly routine or straightforward, depending on the complexity of the income stream.

The common approach to address bonuses, commissions or other variable income streams was to provide that certain documentation would be periodically exchanged, and there would then be a “true-up” in terms of paying the net percentage pursuant to statutory guidelines. The true-up could be as simple as requiring “20 percent of the net income properly calculated” within x days of receipt. The only restrictions on such agreements were that the agreement not be contrary to public policy, unconscionable, or violate section 505(a)(5) of the IMDMA.¹ That section provides that although the guidelines were set up according to percentages of net income, the

final order must state an amount of child support in actual dollar amounts. The practical effect of a child support order that based payments on a percentage of the support obligor’s net income was that child support automatically increased when the payor’s net income increased.

Now that the income share model of child support has been adopted in Illinois, what impact does the change in the law have on these types of variable-income situations? Can agreements still be drafted that effectively respond to these fluctuations, despite the fact that income from both parents must now be considered? Time will ultimately tell, but, for now, the answer appears to be “yes.”

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¹ 750 ILCS 5/505(a)(5) (West 2017)

Before tackling the problems associated with variable income dilemmas, it is critical to have a basic understanding of the primary policy considerations behind the enactment of our new statute. Our new statute was based upon the economic assumption that as income increases, families spend proportionately less money on children, and as such, the old statute had the effect of sometimes creating a windfall to a recipient. Also, an important aspect was the perception of fairness provided by a system that requires consideration of income from two persons, rather than one; the goal with such a system is to avoid dis-incentivizing people from entry into the labor market. With an understanding of the policy implications, the statute can be better understood, enabling more persuasive arguments to a court.

THE INCOME SHARE STATUTE – RELEVANT PROVISIONS

1. “Gross Income”.

The starting point in this analysis is what constitutes “gross income” under the new statute? The answer is found in IMDMA Section 505(a)(3)(A), which provides as follows:

“(3) Income.

As used in this Section, “gross income” means the total of all income from all sources, except “gross income” does not include (i) benefits received by the parent from means-tested public assistance programs, including, but not limited to, Temporary Assistance to Needy Families, Supplemental Security Income, and the Supplemental Nutrition Assistance Program or (ii) benefits and income received by the parent for other children in the household, including, but not limited to, child support, survivor benefits, and foster care payments. Social security disability and retirement benefits paid for the benefit of the subject child must be included in the disabled or retired parent’s gross income for purposes of calculating the parent’s child support obligation, but the parent is entitled to a child support credit for the amount of benefits paid to the other party for the child. “Gross income” also includes spousal maintenance received pursuant to a court order in the

pending proceedings or any other proceedings that must be included in the recipient’s gross income for purposes of calculating the parent’s child support obligation.”

Under the prior version of the statute, questions arose as to what exactly was “gross income,” as the statute did not define the term. Instead, the prior statute provided, in relevant part, as follows: “*Net income’ is defined as the total of all income from all sources, minus...*”

The new income share statute incorporates this concept and provides for a similar definition: “...‘*gross income’ means the total of all income from all sources, except...*”²

Therefore, there is nothing really new here, and what constitutes “income” or “gross income” remains conceptually unchanged, except that now, in determining gross income, maintenance paid is included in the recipient’s income. Further, the term “*all sources of income*” has previously been

interpreted very broadly by the Illinois Supreme Court in *In Re Marriage of Rogers*:³

[T]he first step in calculating a parent’s “net income” is ascertaining “the total of all income from all sources” received by that parent. That determination, in turn, depends on what items may properly be considered “income.” “Income” is not separately defined in Section 505 of the [IMDMA]. We will therefore give it its plain and ordinary meaning.

As the word itself suggests, “income” is simply “something that comes in as an increment or addition * * *: a gain or recurrent benefit that is usually measured in money * * *: the value of goods and services received by an individual in a given period of time.” Webster’s Third New International Dictionary 1143 (1986). It has likewise been defined as “[t]he money or other form of payment that one receives, usu[ually] periodically, from employment, business, investments, royalties, gifts and the like.” Black’s Law Dictionary 778 (8th ed. 2004).

Under these definitions, a variety of payments will qualify as “income” for purposes of section 505(a)(3) of the [IMDMA] that would not be tax-

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² 750 ILCS 5/505(a)(3) (West 2017)
³ *IRMO Rogers*, 213 Ill. 2d 129 (2004)

able as income under the Internal Revenue Code. As our appellate court has recognized, however, the Internal Revenue Code is designed to achieve different purposes than our state's child support provisions. Accordingly, it does not govern the determination of what constitutes "income" under the statutory child support guidelines enacted by the General Assembly.⁴

Rogers, along with other Illinois cases, provides that anything of value can fit under the umbrella of income, including automobile allowances,⁵ IRA distributions,⁶ and moving expenses.⁷ Now, the legislature has codified the concepts of economic value into our statute by declaring that perquisites received, if not included in taxable income, can be included as gross income under IMDMA Section 505(a)(3.1)(B).⁸ The laundry list of examples now in the income shares statute includes, but is not limited to, a company car, housing, housing allowance, and reimbursed meals. All of those items are now on the table for calculating gross income.

2. Variable "Gross Income". Where one parent has variable income sources, or fluctuating income from year to year, calculating his or her "gross income" becomes challenging, and this impacts the other calculations down the line, such as net income. IMDMA Section 505(a)(5)⁹ addresses this issue, and remains largely substantively unchanged from its prior version:

(5) If the net income cannot be determined because of default or any other reason, the court shall order support in an amount considered reasonable in the particular case. The final order in all cases shall state the support level in dollar amounts. However, if the court finds that the child support amount cannot be expressed exclusively as a dollar amount because all or a portion of the obligor's net income is uncertain as to source, time of payment, or amount, the court may order a percentage amount of support in addition to a specific dollar amount and enter such other orders as may be necessary to determine and enforce, on a timely basis, the applicable support ordered.¹⁰

Thus, for cases in which net income cannot be determined because of variances or fluctuations, IMDMA §505(a)(5) still requires that the court provide for reasonable support, in a set dollar amount, but also potentially as some percentage amount. Our appellate

court has addressed handling the issue of variances or uncertainty of income by looking to past income as a harbinger of future income, and includes, in some instances, income averaging as a reasonable solution to determine a support award. Some of the cases dealing with issues of variable income include the following:

- *In re Marriage of Carpel*, which held that fluctuations in husband's income as an attorney working on a contingent basis made it difficult to determine his net income, and that the trial court should consider his previous income to determine his prospective income;¹¹
- *In re Marriage of Garrett*, which held that a 3-year average of the father's income where his income varied significantly from year to year, and the past year's reduction in income was not typical and unexplained;¹²
- *In re Marriage of Nelson*, which held that it was appropriate to average his income over three consecutive years for purposes of child support, because the father's income fluctuated;¹³
- *In re Marriage of Freesen*, which held that the trial court's consideration of only one prior year's income was error when the husband's income varied due to large bonuses, and that the trial court should have averaged income from at least three prior years;¹⁴ and
- *In re Marriage of Pratt*, which affirmed the decision of the trial court to determine the father's estimated annual income from stock dividends by multiplying the first quarter's dividends by four.¹⁵

ISSUES AND STRATEGY UNDER THE NEW STATUTE

The adoption of the income share model adds a new wrinkle to the use of base-plus-percentage orders of support typically relied upon where a payor's income fluctuates. In the past, it was relatively easy to draft orders providing that support would be set at a base amount plus a percentage over that base amount consistent with the child support guidelines. Percentage awards have proved to be a flexible means of adapting support to fluctuating income levels without having to resort to the filing of a petition to modify support as a result of changes in the payor's financial circumstances.

However, it must be kept in mind that under the new provisions, the income of both parents must be considered. Accordingly, this makes it impossible to simply provide in a settlement agreement that the statutorily-required level of support would be paid on an obligor's additional income except in those cases

4 *IRMO Rogers*, 213 Ill. 2d at 136-37 (citations omitted)

5 *In re Marriage of Einstein*, 358 Ill. App. 3d (4th Dist. 2005)

6 *In re Marriage of Lindman*, 356 Ill. App. 3d 462 (2nd Dist. 2005)

7 *In re Marriage of Shores*, 2014 IL App (2d) 130151

8 750 ILCS 5/505(a)(3.1)(B) (West 2017)

9 750 ILCS 5/505(a)(5) (West 2017)

10 *Id.*

11 *IRMO Carpel*, 232 Ill. App. 3d 806 (4th Dist. 1992)

12 *IRMO Garrett*, 336 Ill. App. 3d 1018 (5th Dist. 2003)

13 *IRMO Nelson*, 297 Ill. App. 3d 651 (3rd Dist. 1998)

14 *IRMO Freesen*, 275 Ill. App. 3d 97 (4th Dist. 1995)

15 *IRMO Pratt*, 2014 Ill App (1st) 130465, ¶ 26

where only the obligor is employed. In a case where only the obligor has variable income, it is possible to draft a percentage order based upon the ratio of the obligor's child support obligation to his or her gross income with a further provision that any additional income would be paid as child support based upon that percentage. Yet, even this could be problematic, as the child support obligor could overpay support in the event of substantial income, due to the fact that under the new statute as income increases the relative percentage of support paid decreases.

As another option, it is foreseeable that the use of Family Law Software may become a common practice to help determine the overall percentage of net or gross income that the obligor is paying based upon the income share guidelines considering the income of both parents. Thus, the settlement agreement could provide for mutual disclosure and exchange of income records, and then if the overall percentage no longer corresponds to the prior settlement amount, then child support would be determinable per the guidelines and the matter could then be reviewed as a *de novo* matter.

Because the income share model makes the child support assessment less straightforward than it previously was, the case law regarding income averaging will likely be of great weight. Income averaging can be an appropriate and fair mechanism to employ so as to avoid continuously having to recalculate child support, exchange and pursue financial updates, expend legal fees, and return to court for additional litigation.

When the obligation for child support is not established by a marital settlement agreement, but is set by the court either as a result of a trial or a default hearing, trial courts have on occasion placed a provision in the judgment that required an automatic increase in child support. Such provisions have usually not withstood attack on appeal. The basis for the disapproval of automatic increases in support was well-expressed in the case of *McManus v. McManus*,¹⁶ in which the father was ordered to pay \$70 per month until the child's sixth birthday, \$140 per month until the tenth birthday, \$180 per month until the fourteenth birthday, and \$200 per month thereafter. In that case, the appellate court stated as follows:

In ordering the payment of child support, a circuit court must consider the needs of the child, the separate income of the wife, and the income of the husband. Because changes in these facts cannot be anticipated with accuracy, a circuit court should ordinarily not try to anticipate such changes by making its award of child support to increase automatically with the child's age. The self-adjusting aspect of the award of child support must, therefore, be reversed.¹⁷

16 *McManus v. McManus*, 38 Ill. App. 3d 645 (5th Dist. 1976)

17 *Id.* (citations omitted).

In *Marriage of Moore*,¹⁸ the trial court entered a child support order similar in structure to the order in *McManus*. In *Moore*, the father was a surgeon who had been practicing for approximately four years at the time of the judgment. His income was on the rise. The parties had two minor children. The father was ordered to pay \$1,000 per month, per child, for support, with annual increases of \$1,000 per child per year. The mother urged that the trial court could reasonably expect that the father's income would increase. The appellate court held that the trial court was not entitled to rely on the possibility of a likelihood of future increases in income.

The same principle as in *Moore* and *McManus* was also present in *Coons v. Wilder*.¹⁹ Mr. Coons was a lawyer who had just passed the bar examination. The support order was based on what the father was expected to earn as a lawyer. The support order was reversed on appeal. Similarly, in *Schwartz v. Schwartz*,²⁰ a support order providing for an increase in child support in two years, based on anticipated income that the father would receive from a trust in two years, was reversed.

In contrast to the above disapproved approaches is the approach that was affirmed in *Vollenhover v. Vollenhover*.²¹ In that case, the father's income fluctuated because he received quarterly bonuses. The trial court's decision, which was affirmed on appeal, provided for increases in support payments, which were contingent on the increase in the father's income actually taking place, but it also contained a provision for automatic reduction during those months when the father's earnings decreased. Thus, the *Vollenhover* decision may be cited and relied upon when urging a true-up or true-down under the income sharing amendments, although the age of the case, and the decisional case law that has evolved since 1954 calls into question the weight to be afforded the case.

Moreover, while a substantial change in circumstances pursuant to IMDMA Section 510(a) encompasses a change in income as a basis for a petition to modify support,²² that petition can only affect a prospective modification. If we know a parent typically gets bonuses, or has commission based compensation, overtime or other variable income, here are some potential ways to set child support that adequately accounts for that variability, and does so in certain instances retrospectively.

SOME IDEAS FOR HANDLING VARIABLE INCOME

18 *IRMO Moore*, 117 Ill. App. 3d 206 (5th Dist. 1983)

19 *Coons v. Wilder*, 93 Ill. App. 3d 127 (2nd Dist. 1981)

20 *Schwartz v. Schwartz*, 38 Ill. App. 3d 959 (1st Dist. 1976)

21 *Vollenhover v. Vollenhover*, 4 Ill. App. 2d 44 (1st Dist. 1954)

22 750 ILCS 5/510(a) (West 2017)

1. True-up child support periodically. A true-up agreement could be applied retroactively—*i.e.*, to the past year or other period of time over which child support was paid—or prospectively—*i.e.*, based on the inclusion of the additional income to set child support for the next period of time if it becomes clear that changes to a payor’s income warrant some future adjustment. True-ups can allow for a sense of fairness because the “correct” amount of statutory child support is always being paid, albeit after the fact under these arrangements. They can present some negative challenges as well, including the time, cost, and aggravation of having to continue with obtaining records, running new calculations, and incurring more legal fees in some instances. Regardless, when negotiating a true-up agreement, be certain to include and contemplate the following:

- What is the timing of the true-up (annually, semi-annually, quarterly, annually, etc.)?
- What documents will be used to prove gross income (tax returns, paystubs, schedule K-1s, 1099s, general ledgers, etc.) and how will it be defined?
- Who has the burden of moving forward to prove the correct amount of support?
- How will the computations be done and by whom, and is there a verification process?
- What is the timing for the exchange of information and computations?
- What are the terms of repayment, and whether there will be interest accrual?

Sample Marital Settlement Agreement Language:

“Husband shall pay Wife child support in the amount of \$875 per month. This child support amount is based upon Husband’s gross income of \$100,000 and Wife’s gross income of \$50,000, and the parties’ minor child primarily residing with Wife. The payments shall be made on the first day of each month, commencing December 1, 2017, by Husband to Wife through a direct wire into Wife’s checking account no. XXXX at Chase Bank. The parties acknowledge that Husband’s gross income from employment has fluctuated annually, and that in an effort to achieve consistency within the framework of the Schedule of Basic Child Support Obligation, they have agreed to complete a re-computation or “true-up” of child support each year. To effectuate this “true-up” the parties shall exchange complete federal and state income tax returns within 7 days of filing, together with all schedules and attachments, including, but not limited to, W-2 forms, Schedule K-1s, 1099s, etc., and a year-end paystub from employment. Within the 21 days of exchanging income tax returns, they shall re-calculate the amount of child support that should have been paid under the Schedule of Basic

Child Support Obligation for the prior calendar year based upon the parties’ total gross incomes, as that term is defined under Section 505 of the IMDMA; if there was an overpayment or underpayment of child support, the parties shall “true-up” the overpaid or underpaid amount. Further, in running their child support calculations, the parties shall utilize the Individualized Tax Amount approach pursuant to Sections 505(a)(3)(D), and 505(a)(3)(E) of the IMDMA. The Husband shall be responsible for circulating the initial proposed amount to Wife, together with his calculations and any source backup materials (such as Family Law Software program printouts), and if the parties cannot by agreement resolve the “true-up” amount, then prior to either party proceeding with a petition, they shall immediately employ the services at their equal expense of an agreed-upon neutral accountant to assist in a good faith effort at resolving the “true up” calculation. Once the “true up” amount is agreed upon, or determined by court order if no agreement, the parties shall effectuate the actual “true up” payment within 14 days, with[out] interest.

2. Use predetermined ratios for implementing future child support awards.

In situations where only the obligor has variable income, it is possible to draft a percentage-based order predicated upon the ratio of the obligor’s base child support obligation to his or her total gross income. Any such agreement would include a provision that any additional income (earned above the amount on which the initial child support award was calculated) would be paid as child support based upon that percentage. Remember, however, that there still is a requirement for a specific dollar amount in your child support orders despite this mechanism.

Example: Husband earns \$100,000 per year from his base salary, and receives variable bonuses annually. Wife earns \$50,000 per year and has primary residence of one minor child. Husband’s basic child support obligation from salary alone would be \$875 per month. The ratio of Husband’s child support obligation to his total gross income is 11%. Husband then earns a \$50,000 bonus. Applying the 11% ratio to the gross bonus, results in additional child support of \$458.33 per month on the \$50,000 bonus.

Note: As suggested above, this result is not without fault. It is potentially problematic because the child support obligor, the Husband in the above example, could be overpaying child support in the event of substantial income. Under the same facts above, assuming the total income was simply \$150,000, without any application of the ratios, child support would be a total of \$1,145 per month

compared with \$1,313 in the above example (a difference of \$168 per month).

3. Employ Income Averaging. The income shares amendments make it far more difficult to implement accurate percentage awards of child support, due to a variety of factors, including: (i) as income goes up, the relative support percentages decline; and (ii) the new statute considers the income of both parents. Thus, income averaging may become more prevalent in income variance cases moving forward to avoid constant re-adjustments to child support awards based upon the difficulty both logistically and practically in our cases, and the fact that the case law clearly supports employing income averaging.

See *In re Marriage of Karonis* (holding that the circuit court may consider past earnings in determining the non-custodial spouse's net income for purposes of making a child support award, where it is otherwise difficult to ascertain the net income of a non-custodial spouse).²³ See also *In re Marriage of Hubbs* ("Using an average income for the previous three years of employment is a reasonable method for determining net income where income has fluctuated widely from year to year").²⁴

This approach requires another look at our cases on income averaging to ensure consistency and fairness. In other words, do we employ simple averages, or perhaps, weighted averages more akin to business valuation cases, where it seems one year of income compared to another is determined to be an unreliable predictor of future income (e.g., when the obligor suddenly suffers a suspicious and dramatic drop in income in the year of divorce)?

The other aspect of using income averaging relates to the timeframe over which incomes will be averaged. While three years seems to be a general trend throughout Illinois cases,²⁵ three-year averaging does not necessarily have to be the last three years where there is evidence that a recent downturn in income, attendant to divorce, is atypical.²⁶

4. Determine a predetermined amount or percentage of additional income to be paid as additional child support. While the amount of support changes if net income changes, one can run several alternative scenarios and look realistically at other income results to predetermine additional support amounts to be paid, even if these do not supply precisely accurate predictions of what later occurs. This

²³ *IRMO Karonis*, 296 Ill. App.3d 86 (2nd Dist. 1998)

²⁴ *IRMO Hubbs*, 363 Ill. App. 3d 696 (5th Dist. 2006)

²⁵ See *IRMO Elies*, 248 Ill. App. 3d 1052 (1st Dist. 1993); *IRMO S.D and N.D.*, 2012 IL App (1st) 101876

²⁶ See *IRMO Garrett*, 336 Ill. App. 3d 1018 (5th Dist. 2003).

can always be expressed as additional dollar amounts or percentages on different ranges of income. A helpful tool in analyzing different child support scenarios is to run alternative options through the Guideline "What If" worksheet in Family Law Software. This allows you to change variables for child support, including various income levels, to see how it modifies the child support obligations in amount and allocation.

5. Provide for permissive modifications retroactively in the agreement. If this is an agreement, there is no reason why the bar to retroactive modifications could not be waived in certain well-defined circumstances. The agreement can provide for periodic production or exchange of income information, and permit either party to trigger a review of the support amount for a prior period with specific terms for any shortfall or overpayment.

6. Work outside the confines of guideline support. In addition, while the new income share provisions now apply to all child support determinations, there can still be deviations from the guidelines (as long as appropriate findings are made and the actual support amount is referenced). For negotiated cases, consider whether support guidelines have any meaningful application, or whether the family's best interests might be served by allocating or sharing payment of the children's direct and indirect expenses rather than an arbitrarily-defined child support amount. While the support amount is supposed to reflect expenditures (for an intact family) at various income levels for the children, those statistical averages may not in any way reflect your client's family's expenditures. Consider moving outside these defined amounts to allow the clients to make their own agreements in mediation, collaborative, or other settlement processes.

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