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## Tax bill may upset spousal maintenance

Changes in the law over time are a necessary part of the legal process, but can be particularly difficult for divorcing parties. Changes in laws that affect divorce can require parties to make difficult choices that impact their families and financial future based on educated predictions about application of brand new laws or laws that have not yet gone into effect.

For example, the maintenance provisions of the Illinois Marriage and Dissolution of Marriage Act have undergone several changes in the last few years, and there are more to come.

The first major change to the maintenance statute in many years occurred in January 2016 when the statute was amended to provide guidelines for the amount and duration of maintenance in certain cases.

Prior to the enactment of the guidelines in January 2016, all maintenance awards were based on the factors set forth in Section 5/504 of the marriage act and subject to the court's broad discretion. While case law provided insight on application of the statutory factors, maintenance awards varied significantly among districts and judges.

The January 2016 amendments to the act provide a formula for calculation of amount and duration of maintenance for parties with a combined gross income of less than \$250,000 per year, after a baseline determination that a maintenance award is appropriate. While the statute still grants discretion for deviation from the guidelines, the January 2016 amendments provide greater predictability for the range of outcomes, particularly for those parties with combined

gross annual income of less than \$250,000.

Maintenance awards where combined gross income is \$250,000 or more annually remain subject to the factors in the maintenance statute; however, judges may still apply the new guidelines, or a portion of the guidelines, in awarding maintenance in higher-income cases.

For example, a judge may apply the guidelines for duration of maintenance in a higher-income case, but not apply guidelines for the amount. It is difficult to predict whether and how a judge might apply the current guidelines in higher-income cases. This means that parties may be forced to decide on strategy with limited insight into the effect of the current guidelines on their case.

In yet another change to Illinois law, a further amendment to the maintenance provisions of the marriage act is scheduled to take effect in June that, among other changes, will raise the ceiling for application of the guidelines to parties with combined annual gross income of less than \$500,000. The June 2018 amend-

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ment also will allow for crediting of court-ordered temporary maintenance payments toward final maintenance awards and will further refine the duration provisions.

The most significant legal change regarding maintenance with the potential to impact divorcing parties in recent memory is the tax reform bill proposed by

### MODERN FAMILY



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the U.S. House of Representatives.

The Internal Revenue Code provides a significant financial benefit to divorcing parties due to an arbitrage effect created by payment of spousal maintenance by a payor in a high tax bracket to a recipient in a lower tax bracket. Maintenance can be included in the income of the recipient and is deductible from the income of the payor.

Simply put, the payor is actually paying less than his or her gross obligation because of the higher tax saved with the maintenance deduction.

The recipient is receiving taxable income as maintenance but the recipient's tax is less due to being in a lower bracket. The taxes saved using the arbitrage may be allocated between the

parties when they compute the amount of maintenance to be paid.

In most cases, there is not enough available net income to allow families to maintain the same standard of living post-divorce that existed prior to the divorce. Current tax law may help buffer the impact of income being divided between two households by increasing the total net income.

The tax reform bill proposed by the U.S. House would dramatically alter the tax impact of spousal maintenance payments by eliminating the tax impact to both the payor and recipient, so maintenance would be tax neutral to both parties. There will no longer be a tax savings to share, making it more difficult to support two households on one income.

To further complicate matters, maintenance in Illinois and many other states is calculated based on gross income, due in part to the tax impact of maintenance under current federal law.

If maintenance is not deductible from the income of the payor, the pool of money the payor has from which to pay maintenance will be smaller. If state law lags behind changes to federal law, inequity can be the result.

For example, a payor with less net income may be unable to pay the maintenance required under a judgment. In addition, nontaxable maintenance may create an unintended windfall to the maintenance recipient.

If the House tax reform bill becomes law, additional new legislation in all states will be needed to remedy these as well as other problems that would arise.