



7. Taxpayer submitted a copy of a Consent Decree of Dissolution of Marriage (Decree) signed November 8, 2010 regarding Taxpayer and Wife.
8. Paragraph 4.b. of the court's order required Taxpayer to pay alimony of \$[REDACTED] per month beginning the month after the Decree was signed.
9. Paragraph 4.b. also provided that the payments are to be included in Wife's income and deductible by Taxpayer and that the payments would end if Wife is remarried or deceased.
10. Based on the additional information the Section issued a modified proposed assessment dated June 24, 2015 allowing Taxpayer an alimony deduction of \$[REDACTED].
11. Exhibit A to the Decree related to property and debts of Taxpayer and Wife. Paragraph 3 of Exhibit A provided that each party is awarded his/her interest in any and all retirement benefits, pension plans or other deferred compensation.
12. Taxpayer testified at the hearing that the approximately \$[REDACTED] he paid to Wife and deducted as alimony represented a distribution of one-half of their total combined retirement accounts. Because Taxpayer had more money in his retirement account, the payment was intended to result in a distribution of 50% of the combined amount to each spouse.
13. The Section contended at the hearing that the payment was a property settlement and did not qualify as alimony payment under the Internal Revenue Code (I.R.C.).

#### CONCLUSIONS OF LAW

1. Arizona Taxpayer may deduct on their Arizona income tax return itemized deductions calculated under the Internal Revenue Code. Arizona Revised Statutes (A.R.S.) § 43-1042.
2. I.R.C. § 215(a) allows a deduction for alimony or separate maintenance payments paid during the taxable year.

3. I.R.C. § 215(b) defines alimony or separate maintenance payments as any alimony or separate maintenance payment defined in section 71(b) which is includible in the gross income of the recipient under section 71.
4. I.R.C. § 71(b)(1) defines alimony or separate maintenance payments as:
  - (A) payments received by (or on behalf of) a spouse under a divorce or separation instrument,
  - (B) the divorce or separation instrument does not designate payment as a payment which is not includible in gross income under section 71 and not allowable as a deduction under section 215,
  - (C) in the case of an individual legally separated from his spouse under a decree of divorce or of separate maintenance, the payee spouse and the payor spouse are not members of the same household at the time such payment is made, and
  - (D) there is no liability to make any such payment for any period after the death of the payee spouse and there is no liability to make any payment (in cash or property) as a substitute for such payments after the death of the payee spouse.
5. Paragraph 3 of Exhibit A did not provide that there would be no liability for a payment to be made after the death of Wife.
6. Payments made by Taxpayer pursuant to Paragraph 3 of Exhibit A did not meet the definition of alimony or separate maintenance payments and were not deductible under I.R.C. § 215(a).
7. The payments under Paragraph 3 of Exhibit A were therefore not deductible under A.R.S. § 43-1042 for Arizona income tax purposes.

8. A.R.S. § 42-1123(C) provides that if the tax “or any portion of the tax is not paid” when due “the department shall collect, as a part of the tax, interest on the unpaid amount” until the tax has been paid.
9. A.R.S. § 42-1123(C) recognizes the time value of money, and thus requires a taxpayer that is holding or using money that rightfully belongs to the State to pay interest for the use of that money. *Valencia Energy Co. v. Arizona Dep't of Revenue*, 191 Ariz. 565, 959 P.2d 1256 (1998).
10. The Section’s modified proposed assessment dated June 24, 2015 is upheld.

### DISCUSSION

The issue in this case is whether Taxpayer may deduct payments of \$[REDACTED] made by Taxpayer to Wife. The payments represented a division of their combined retirement accounts. Because Taxpayer had more money in his retirement account, the payment was intended to distribute 50% of the combined amount to each spouse.

Arizona taxpayers may deduct on their Arizona income tax return itemized deductions calculated under the Internal Revenue Code. I.R.C. § 215 provides a deduction for alimony. I.R.C. § 71(b) requires that the four conditions listed in Conclusions of Law No. 4. be met before a payment may be deducted as alimony. Taxpayer’s payment does not meet the fourth condition, that the obligation to make payments stops on the death of the payee spouse (Wife in this case).

Paragraph 3 of Exhibit A to the Decree awarded each party his/her interest in any and all retirement benefits, pension plans or other deferred compensation. The Exhibit did not award the Wife monthly payments or explicitly provide that payments would terminate upon Wife’s death. By contrast, Paragraph 4.b. of the court’s order specifically provided that the payments under that paragraph are to be included in Wife’s income and deductible by Taxpayer and that the payments would end if Wife is remarried or deceased.

The modified proposed assessment included interest. A.R.S. § 42-1123(C) provides that if the tax "or any portion of the tax is not paid" when due "the department shall collect, as a part of the tax, interest on the unpaid amount" until the tax has been paid.

Interest is not a penalty, but is simply compensation to the state for the lost time-value of money received after the due date. *Valencia Energy Co. v. Arizona Dep't of Revenue, supra.* (Non-punitive interest is, after all, nothing more than compensation for the use of money. The taxpayer had the benefit of using the funds before paying the tax claim and, in the legal sense, suffers no loss by reason of paying interest on the money it retained in its possession.)

Based on the foregoing, the Section's modified proposed assessment dated June 24, 2015 is affirmed.

DATED this 2nd day of June, 2016.

ARIZONA DEPARTMENT OF REVENUE  
HEARING OFFICE

[REDACTED]  
Hearing Officer

Original of the foregoing sent by  
certified mail to:

[REDACTED]

Copy of the foregoing delivered to:

Arizona Department of Revenue  
Individual Income Tax Audit Section