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Tax Issues to Look Out for in a Divorce in New Jersey

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There's an old saying that the only sure things in life are death and taxes. Hopefully, death is a long way off, but sadly, taxes are here with us front and center. In the divorce process, the issue of taxes is something that is considered in several stages.

Filing Taxes After Divorce in NJ

First, your tax status (married filing jointly, single, head of household, etc.) is based on your status on December 31 of any given year. The timing of an actual divorce can be important to maximize dollars. For example, suppose you have been filing married filing jointly during the marriage. Chances are, your withholdings from an employer are calculated based on that filing status. When your marriage is dissolved, you will have to file as single (or head of household- but more on that later). Suppose you are divorced late in the year. In that case, this could result in a significant amount being owed to Uncle Sam because of having withholdings for the majority of the year based upon filing married, but actually having to file single. One way to mitigate this is to hold off on the actual divorce until after January 1 of the new year. If you have settled your case, and it is towards the end of the calendar year, it may be possible to wait until the first part of next year to be divorced. You should discuss the options of holding off on your divorce with your accountant and your lawyer to identify what is best for you and your family.

Divorced Parents Claiming Children on Taxes in NJ

Children come with many joys, lots of worrying, and a myriad of tax considerations in a divorce or break up. First, an important consideration when children are involved in a divorce is how the parents will share the tax benefits of children. Who will claim the child, or children, as dependents? If both parents meet the IRS criteria for claiming a child, a court will most often allow the parents to share this. If there is one child, the parents will alternate, and if there are two, each will claim one, and then alternate when the oldest child can no longer be claimed. The ability for parents to claim a child is often dependent on child support and related expenses being current.

Child Support and Taxes After Divorce in NJ

Another tax consideration with children is in the calculation of child support. Child support is based largely on the net available income (after taxes) of the parents. If the paying parent is going to be sharing the dependency allowance for the child or children, this needs to be factored into the child support. Most courts and attorneys use software to calculate support, and without attention, the computer will often make assumptions, including filing status, and who claims the child(ren) as a dependent. If you do not pay close attention to these inputs, the paying parent may be assessed an incorrect (and too high) amount of taxes, resulting in less net income and a lower child support amount.

New Jersey Tax Law on Alimony

In 2018, the tax laws changed, and alimony is no longer taxable to the recipient and deductible to the person paying. However, this does not necessarily end the query. Alimony is based on several factors, including what amount of money is needed by the recipient. If one party has significant tax issues, this can be considered.

Equitable Distribution and Taxes After Divorce in NJ

There are many issues of taxes and equitable distribution in a divorce, and it is impossible to discuss all of them in a single blog. However, there are specific issues to be aware of and to consult with your accountant and lawyer before entering into any agreement or taking a position at trial with regard to any particular asset. Indeed, the divorce laws of New Jersey specifically require a judge to consider tax consequences when making an equitable distribution of assets.

It is easy to just add up the values and “horse trade” assets. In other words, let’s say all the assets equal $2,000,000. One spouse takes the house and the brokerage accounts, and the other takes the retirement accounts and the money market accounts. Sounds good, but what may not have been considered is that the brokerage account may be worth $600,000, but it is comprised of Tesla stock that was purchased when the company started and rose substantially in value. The sale of that stock will be a transaction that results in significant taxes, so the spouse who thought they might be getting $600,000 may be getting significantly less after taxes. Meanwhile, the retirement account has not been taxed, but depending on when it will be liquidated, the net amount will change depending on the then tax rate of the account holder. Carrying forward losses and capital gains are also important issues that must be addressed to ensure that there is no unfair benefit or detriment to either party in a divorce.

These are just a few examples of why it is so essential to make sure your lawyer is aware of these issues, and a financial adviser or accounts is consulted when discussing equitable distribution.

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