

Deduction from incomes in the child support formula

Unintended consequences and how to deal with them

by Shuneet Thomson

September 27, 2009

Designing a child support formula that addresses all concerns is very hard, if not impossible. We know this to be true, because no matter how much hard work child support taskforces have invested over the years in designing the child support formulae, each new formula inevitably has new limitations along with its good points.

Until the current child support guidelines (CSG) are revisited in a few years, we need to find ways to address some concerns that have emerged. In this paper I would like to highlight the consequences of deducting various expenses from the parties' incomes in the first part of the formula. I realize that this approach is taken in the child support formulae of other states, but that does not necessarily mean it is a good idea.

Readers need to understand that the effects of these deductions, as described here, contribute to the outcome of the calculation any time parties make the deductions, even when other factors, such as a large difference in income, obfuscate these effects or even override them.

Readers might benefit from having the CSG worksheet on hand when reading this paper. You might also want to familiarize yourself with two items on the worksheet, to which I will refer repeatedly:

- Item 1g on the worksheet: the "Combined Available Income" or in short "the Available income."
- Item 2a on the worksheet ("combined amount for one child"), to which I will refer as the "Joint child-Related Budget" or, in short, the "Children's Budget."

A. Assumptions

To be able to isolate the consequences for child support of the deductions from the parties' incomes (items 1b through 1e on the worksheet), other variables need to be held constant. In this paper the following assumptions will apply in all examples that are given:

1. Examples will apply to one child.
2. Parties' incomes will be equal, and
3. I will assume the Joint Children's Budget (item 2a on the worksheet) is figured as 20% of the parties' Combined Available Income, although this percent varies in reality, and tends to be higher.

It should be noted that the points made here are as valid when there is more than one child and just as valid when the percent of the Children's Budget out of the Available Income is other than 20%.

Lastly, for the sake of discussion, as most Payors of CS are men, I will assume a paying father (the Payor) and a recipient mother (the Recipient).

B. The consequences of deductions from the parties' incomes

In the worksheet, the deductions out of each party's income have two consequences, or "effects."

One, the deductions drive child support downwards. By reducing the Available Income, the deductions reduce the Children's Budget, which in the end leads to lower child support. I will call this effect the "**Available Income Effect**" of the deductions.

Two, by reducing each party's available income, deductions from income also affect the *ratio* that each party is expected to contribute to the Joint Children's Budget. The smaller the portion of the Recipient's income out of the Available Income, the less she is expected to contribute to the Children's Budget and therefore the more child support she gets, and vice versa. I will call this the "**Ratio Effect**" of the deductions.

Deducting medical and support payments from incomes and thereby reducing the Children's Budget must have been the Taskforce's reasonable intention. What is probably an unintended consequence is how differently this part of the formula affects the parties. These outcomes are illustrated in Table I.

**TABLE I: THE 2009 CHILD SUPPORT GUIDELINES:
EFFECT OF DEDUCTIONS FROM PARTIES' INCOMES
ON THE PAYOR VS. THE RECIPIENT OF CHILD SUPPORT ***

	<u>Deductions by</u>		<u>Combined Avail.</u>	<u>Joint child</u>	<u>Income ratio</u>	<u>C.S.</u>
	<u>Payor</u>	<u>Recipient</u>	<u>Income</u>	<u>budget</u>	<u>Payor / Recipient</u>	<u>Order</u>
1	-	-	\$2,000	\$454	50 : 50	\$227
2	-	\$150	\$1,850	\$426	54: 46	\$230 (+ \$3)
3	\$150	-	\$1,850	\$426	46 : 54	\$196 (- \$31)
4	-	\$300	\$1,700	\$397	59 : 41	\$234 (+ \$7)
5	\$300	-	\$1,700	\$397	41: 59	\$163 (- \$64)

* *Assumptions:* \$1,000 income per party per week, and one child.

Consider Table I:

Line 1 in Table I presents a base line – the Parties each earn \$1,000, and no deductions are taken from their incomes; the child support indicated in lines 2-5 of Table I is compared to the child support indicated on the base line.

In Line 2 the Recipient deducts \$150, the Payor deducts none. Her ratio of out of the Combined Available Income is 46%. Child support goes up (relative to the baseline) by \$3 a week.

In line 3 the *Payor* deducts \$150, and the Recipient deducts none. His weekly child support drops by \$34 (eleven times greater savings for Payor than for Recipient, after deducting the same amount).

Lines 4 and 5 provide a similar illustration with deductions of \$300 respectively. When the Recipient deducts \$300, all she gets is \$7 a week more (compared to no deductions on the base line). When the Payor deducts \$300, his child support drops by \$71 a week (ten times greater savings than the Recipient's).

How can one understand these numbers? Why did the same deduction from the same income benefit the Payor about ten times more than the Recipient? The explanation lies in the divergent outcomes for Payor and Recipient caused by the two “effects” of the deductions from incomes, as explained next.

1. *The Available Income Effect:*

The most significant feature of the Available Income Effect is that it is induced by the deductions from the parties' incomes *irrespective* of whether the deductions come out of the Payor or the Recipient's income. The impact of deductions from the incomes of *either* party is a reduced child support.

The Payor benefits from the deductions from his income (which is the intention) *and* from the deductions out of the Recipient's income: the more deductions from either income, the better for the Payor, because his child support is reduced by reducing the parties Available Income, out of which the Children's Budget is drawn.

The advantage that the Payor gains from the Recipient's deductions represents a disadvantage for the Recipient of child support. Her interest is usually to get as much support as possible; however, it appears that the more she deducts, the less child support is indicated initially by her deductions.

The “Ratio Effect” is designed to correct this outcome, because the deductions from the Recipient's income also reduce her portion of the Children's Budget and thereby increase the Payor's portion, i.e., increases child support. But does the Ratio Effect benefit her as much as it benefits the Payor?

2. The Ratio Effect

Unfortunately, here too the effect on the Payor and on the Recipient is different.

On the worksheet, when the *Payor* deducts expenses from his income, his reduced income lowers his ratio out of the Children's Budget, and therefore reduces his child support order. The Payor's Ratio Effect *compounds* the advantage he gained from the lowered Available Income and produces a significant reduction of his child support order, as seen in Table I.

For the *Recipient* of child support, the deductions from her income lower her ratio out of the Children's Budget and benefit her – but only very little: most of the increase in child support that is indicated by her Ratio Effect is erased by the negative consequence for her of the Available Income Effect. As seen in Table I, the increase in child support that she gains from her deductions from income is ten times smaller than the reduction in child support that the Payor gains by deducting the very same amount.

The examples in Table I show only one party taking deductions from income. If both parties have deductions, the Recipient's disadvantage is even greater, because the Payor's deductions add substantially to his advantage and can override any benefit she gets from the Ratio Effect of her own deductions. She could end up gaining no benefit at all, or even getting less child support as a result of her deductions.

Here, for example, is how these paradoxical effects manifests in the deduction of health insurance premiums.

C. The new CS Guidelines and health insurance premiums

In the former child support formula, half the premium for a family health insurance plan that covered both parties and their children was added or deducted from child support, depending on who carried the family health insurance plan. If each party had a policy of their own, half the cost of adding the children on one of their policies was usually added (or deducted) from child support. That seemed fair, and could be disregarded if one Party's income was too low to afford their share of the premium.

Assuming the Children's Budget is figured as 20% of the Parties' Available Income, what is the outcome of deducting the premium by either Party? As illustrated above, the outcome for the parties is different.

When the *Payor* of child support deducts his family health insurance premium from his income on the worksheet, as we know, it reduces the Available Income. If the Children's Budget is 20% of the Available Income from which the premium has been deducted, then the Children's Budget will be smaller by 20% of the premium (compared to the Children's Budget if the premium was not deducted).

Here is a numeric illustration of this arithmetic point.
Assuming the parties' income before any deduction is \$2,000:

1. When no deductions are taken from the incomes
 $20\% \times \$2,000 = \400 Children's Budget.
2. When a premium of \$200 is deducted from a party's income -
 $20\% \times (\$2,000 - 200) = 20\%$ of \$1,800 = \$360 Children's Budget.
The Children's Budget is reduced by \$40, which is 20% of the \$200 premium that was deducted.

As child support is only a portion of the Children's Budget, it means that deducting the health insurance premium has reduced child support for the Payor by less than 20% of the health insurance premium (in this example). That is 20% or less, not 50% as it used to be.

If the *Recipient* of child support carries the family health insurance, not only does she not get an additional contribution in the child support order towards her premium, her child support could actually be *reduced* for the same computational reason it is reduced for the Payor. It is reduced by the Available Income Effect and then the reduction is compensated for by the Ratio Effect. She either gets a very slight increase in child support by deducting the premium from her income, or – depending on the Payor's deductions, she might even get less child support as a consequence of deducting the premium. One thing is sure – deducting the health insurance premium as part of the child support calculation will not lead to a 50% participation in the premium by the Payor.

D. Implications

What are the practical implications?

Where health insurance premiums are concerned, it looks like, in fairness, the health insurance premiums should not be included in calculating child support (*leave it at zero*), unless the income ratio is such that the party paying the health insurance premium does not mind getting much less than half the premium contributed by the other party. If the party who carries the family on his/her plan would like the other party to contribute half the premium, we may have to deal with health insurance premiums separately under the clause in the memorandum that deals with health insurance. This is especially relevant if the insuring party is the Recipient.

Parties usually want to deduct as much as possible from their respective income on this formula. Maybe we are conditioned by tax return filings to consider it an advantage to deduct as much as possible from our incomes. Maybe parties also see in the deductions public recognition of the fact that they are spending this money on their children. However, as we've seen, whereas the deductions serve the Payor's interests very well, the Recipient in particular might need to be disabused of the notion that the deductions from her income are beneficial for her.

One conclusion could be that we have to test different scenarios with our clients, so they have a full understanding of the implications of this formula and can adapt it to their particular situation.

Ultimately the child support guidelines are a thoughtful attempt to find a child support formula that is fair to both parents and to the children. However, there are built in assumptions that render this formula and others that preceded it inherently unfair. Churchill once said "Success is going from failure to failure without a loss of enthusiasm." I don't think the word "failure" applies to this or any other child support formula, but we do need to hold on to the "enthusiasm." So, here is to keeping the enthusiasm going as we explore the child support conundrum.