

Defining “Income” for Child Support

[Updated and supplemented from Child Support Chapter of District Court Bench Book]

A. Determining a parent’s child support obligation under Guidelines.

1. The first step in determining a parent’s child support obligation under the Child Support Guidelines is to determine each parent’s **gross income**.

2. Although North Carolina’s schedule of basic support obligations is based on net income (gross income minus federal and state income and payroll taxes), the net income ranges have been converted to gross income ranges by factoring in federal and state income and payroll taxes.

3. A parent’s child support obligation should be based on the parent’s actual income at the time the child support obligation is determined, unless grounds exist to impute income. [*Frey v. Best*, 189 N.C. App. 622, 659 S.E.2d 60 (2008)(error to base child support on income earned in the past; child support must be based on present actual income unless there are grounds to impute income); *State ex. rel. Godwin v. Williams*, 163 N.C. App. 353, 593 S.E.2d. 123 (2004)(error for trial court to use earning capacity of full time college student rather than his actual income without finding grounds to impute income); *Hodges v. Hodges*, 147 N.C.App. 478, 556 S.E.2d 7 (2001) (trial court erred when it included income from a part-time job parent no longer held when order entered)].

a) Order must contain a finding of actual income at time order is entered. [*Armstrong v. Droessler*, 177 N.C. App. 673, 630 S.E.2d 19 (2006)]

b) However, it may be appropriate to use evidence of past income to determine present income. *Hartsell v. Hartsell*, 189 N.C. App. 65, 657 S.E.2d 724 (2008)(no error for trial court to use plaintiff’s actual earnings during year prior to hearing despite testimony from plaintiff that he was not likely to continue earning that amount); *but cf. Glass v. Glass*, 131 N.C. App. 784, 509 S.E.2d 236 (1998)(error for trial court to conclude income would stay the same as previous years despite finding obligor would not receive bonuses that he had received in the past); *Holland v. Holland*, 169 N.C.App. 564, 610 S.E.2d 231 (2005) (error to use 2001 income for 2002 order, however, court of appeals noted that with

appropriate findings the trial court could have used the 2001 information to set a figure for 2002); *Deihl v. Deihl*, 177 N.C. App. 642, 630 S.E.2d 25 (2006)(trial court did not impute income when it averaged incomes from past years to determine present income); *See also Squires v. Squires*, 178 N.C. App. 251, 631 S.E.2d 156 (2006)(allowed court to average past income in alimony case). *Cf. Conrad v. Conrad*, 252 N.C. 412 (1960)(trial court is not allowed to select a single year in the past nor average income from several years if that amount does not fairly represent an obligor's present income)].

c) The court of appeals has approved using evidence of expenditures to help prove actual income of a party. [*See Ahern v. Ahern*, 63 N.C. App. 728, 306 S.E.2d 140 (1983); *DeBruhl v. Debruhl*, unpublished opinion, 168 N.C. App. 595, 608 S.E.2d 416 (2005)(used actual expenditures to find amount to impute to obligor). *See also Dillon v. Rains*, 193 N.C. App. 208, 666 S.E.2d 800 (2008)(opinion acknowledges without comment that trial court used expenditures to support finding of actual income)].

4. The second step is to determine allowable deductions from a parent's gross income to get his or her **adjusted gross income**. A parent's presumptive child support obligation is based primarily on his or her adjusted gross income.

5. Finally, if applicable, **adjustments** to a parent's basic child support obligation are made: certain expenditures may be added to the obligation and prorated between the parties and certain deductions may be subtracted from the obligation.

B. Gross income.

1. Gross income is income before deductions for federal or state income taxes, Social Security or Medicare taxes, health insurance premiums, retirement contributions, or other voluntary or mandatory amounts withheld from a parent's income. [2006 and 2011 Guidelines][2011 Guidelines apply to cases heard on or after January 1, 2011; 2006 Guidelines apply to cases heard before that date]

2. The determination of income is a conclusion of law rather than a finding of fact. [*State obo Midgett v. Midgett*, 680 S.E.2d 876 (N.C. App. 2009), *citing Lawrence v. Tise*, 107 N.C. App. 140 (1992).]

3. Income has been construed broadly by the court of appeals. [*See e.g. Spicer v. Spicer*, 168 N.C. App., 607 S.E.2d 678 (2005)(designating all of a personal injury settlement as income, rejecting argument that part of award compensating pain and suffering should be excluded)]

4. Gross income includes:

a) Income from any source. [2006 and 2011 Guidelines]

b) Alimony received by a parent from someone who is not a party to the pending child support action. [2006 and 2011 Guidelines]

- c) Personal injury awards. [*See Spicer v. Spicer*, 168 N.C. App. 283, 607 S.E.2d 678 (2005) (including income from personal injury settlement and rejecting argument that awards compensating “pain and suffering” should be excluded from definition of income).]
- d) Social security benefits received for the benefit of a child as a result of the disability or retirement of either parent is income to the parent on whose earnings record the benefits are paid. [2006 and 2011 Guidelines]
- (1) The amount of the benefit is deducted from the parent’s child support obligation.
 - (2) Earlier versions of the guidelines provided otherwise. [*See* N.C. CHILD SUPPORT GUIDELINES, 1999 ANN. R. N.C. 32 (effective October 1, 1998) and *Sain v. Sain*, 134 N.C.App. 460, 517 S.E.2d 921 (1999) (guidelines prohibited trial court from considering disability payments received on behalf of a child as income in determining presumptive support amount).]
- e) Social security retirement or disability benefits that are received by a parent for the parent. [2006 and 2011 Guidelines]
- f) Child support payments received by the parent for other children residing in that parent’s home. *Dillon v. Rains*, 193 N.C. App. 543, 660 S.E.2d 800(2008)(noting that obligor’s responsibility for the support of other children is deducted from the child support obligation). *But see* 2011 Guidelines, applying to cases heard on or after January 1, 2011 (income received by parent for other children is excluded from income. See discussion below)]
- g) Veterans’ benefits, military pensions and retirement benefits, military pay and allowances, state and federal retirement benefits, and other pensions and annuities. [2006 and 2011 Guidelines]
- h) Workers’ Compensation benefits. [*Felts v. Felts*, unpublished opinion, 192 N.C. App. 543, 665 S.E.2d 594 (2008)(trial court properly awarded portion of lump sum worker’s compensation settlement to custodial parent as child support)].
- i) In-kind goods and services, such as free housing or use of a company car received by a parent in the course of employment, self-employment, or operation of a business may be counted as gross income if they are significant and reduce the parent’s personal living expenses. [2006 and 2011 Guidelines; *Leary v. Leary*, 152 N.C.App. 438, 567 S.E.2d 834 (2002) (no error when trial court added \$250 per month to father's gross income since he had the benefit of a company car).]
- j) Cost-free housing has been considered a form of gross income, as has the payment of rent by a relative. [*Spicer v. Spicer*, 168 N.C. App.

283, 607 S.E.2d 678 (2005) (trial court did not err in including as income \$300 per month, which was the value of father's free housing from his parents); *Williams v. Williams*, 179 N.C. App. 838, 635 S.E.2d 495 (2006)(rent payments paid by grandparents must be included in custodial parent's income.) *But cf. Brown v. Brown, unpublished opinion*, 192 N.C. App. 734, 666 S.E.2d 217 (2008)(trial court did not err when it refused to impute rental income to dependent spouse in alimony case for adult child living in her home)]

k) A friend's consistent and recurring deposits into a parent's bank account, when parent provided no documentation or other evidence supporting his claim that deposits were loans, considered income to that parent either as a gift or as maintenance. [*Onslow Cty obo Eggleston v. Willingham, unpublished opinion*, 687 S.E.2d 541 (N.C. App., 2009).]

l) In an alimony case, court of appeals has held that recurring payments from relatives or other third parties must be included in income if the payments are "reliable" and "contribute to household expenses." [*Dodson v. Dodson*, 190 N.C. App. 412, 660 S.E.2d 93 (2008)(considering payments received by dependent spouse from her adult children). *Cf. Easter v. Easter*, 344 N.C. 166 (1996)(payments from third parties should be factors to consider in deviation).]

m) Educational loans obtained to attend college may be income if loans are not "means tested" assistance and the loans reduce living expenses. [*McKyer v. McKyer*, 179 N.C. App. 132, 632 S.E.2d 828 (2006)].

5. Gross income does not include:

a) Alimony that is received by a parent from a spouse or ex-spouse who is the other parent involved in the pending child support action.[2006 and 2011 Guidelines]

b) Beginning with cases heard on or after January 1, 2011, child support payments received on behalf of a child other than the child for whom support is being sought. [2011 Guidelines].

c) Income earned by or attributable to a parent's current spouse or person living with the child's parent. [2006 and 2011 Guidelines; *see Kennedy v. Kennedy*, 107 N.C.App. 695, 421 S.E.2d 795 (1992) (father considered to have received only one-half of rental income from property held as tenants by the entirety with his current wife).]

d) Means-tested public assistance payments received by a parent, which includes temporary assistance for needy families (TANF or Work First), food stamps, and supplemental security income (SSI) and general assistance. [2006 and 2011 Guidelines]

e) Adoption assistance subsidies for special needs children are not income of the parents but constitute money received by the children. [*Gaston County ex rel. Miller v. Miller*, 168 N.C. App. 577, 608 S.E.2d 101 (2005) (such payments are a resource of the adopted child, not a subsidy to the parents).]

f) Proceeds received in exchange for assets. [See *McKyer v. McKyer*, 179 N.C. App. 132, 632 S.E.2d 828 (2006)(Proceeds from the sale of a home is not “non-recurring” income; court indicated there might be income if the sale resulted in a gain but noted the lack of evidence of a gain; and *Ross v. Ross, unpublished opinion*, 193 N.C. App. 247, 666 S.E.2d 889(2008)(lump sum payment received by wife when she was terminated from her employment was not severance pay because it was payment for release of contract rights; as such, the lump sum payment was not income). *But cf. Hartsell v. Hartsell*, 189 N.C. App. 65, 657 S.E.2d 724 (2008)(court of appeals states that proceeds from the sale of a truck should be included as “income from any source.”)]

g) Payments made by an employer on behalf of an employee for Social Security and Medicare taxes that are not deducted from the salary of the employee. [*Caskey v. Caskey*, 698 S.E.2d 712(N.C. App., 2010)(for cases filed before effective date of 2011 Guidelines); 2011 Guidelines (for cases heard on or after January 1, 2011).]

h) Amounts paid by parent’s employer directly to a third party or entity for health, disability or life insurance or retirement benefits and are not withheld or deducted from the parent’s wages, salary or pay. [2011 Guidelines. For cases heard before January 1, 2011, *see Caskey v. Caskey*, 698 S.E.2d 712 (N.C. App., 2010).]

6. Income from self-employment or operation of a business.

a) In the case of income derived from self-employment, rent, royalties, ownership or operation of a business, or joint ownership of a partnership or closely held corporation, gross income is gross receipts minus ordinary and necessary expenses required for self-employment or business operation. [2006 Guidelines and 2011 Guidelines]

b) Income from self-employment or operation of a business includes or may include:

(1) Undistributed net income of a closely-held (Subchapter C) corporation or partnership may be attributed to a parent who is a shareholder or partner if the parent could require distribution by virtue of the parent’s legal interest in the corporation or partnership and retention of the income by the corporation or partnership is not reasonably necessary for business purposes. [*See Cauble v. Cauble*, 133 N.C.App. 390, 515 S.E.2d 708 (1999) (father owned a

controlling corporate interest so that he might have directed distribution of corporate profits to his benefit).]

(2) Payments and reimbursements (including in-kind goods and services, such as free housing or use of a company car) received by a parent in the course of employment, self-employment, or operation of a business may be counted as gross income if they are significant and reduce the parent's personal living expenses. [2006 and 2011 Guidelines; *Leary v. Leary*, 152 N.C.App. 438, 567 S.E.2d 834 (2002) (no error when trial court added \$250 per month to father's gross income since he had the benefit of a company car).]

c) Ordinary and necessary business expenses.

(1) Ordinary and necessary business expenses do not include accelerated depreciation or investment tax credits or any other business expenses determined by the court to be inappropriate for determining gross income. [2006 and 2011 Guidelines; *Lawrence v. Tise*, 107 N.C.App. 140, 419 S.E.2d 176 (1992) (per the guidelines, accelerated depreciation is not to be deducted from a parent's gross income as an ordinary and necessary business expense); see also *Holland v. Holland*, 169 N.C.App. 564, 610 S.E.2d 231 (2005) (trial court erred in treating all depreciation as accelerated depreciation which, under *Tise*, is not allowed as a deduction from a parent's business income).]

(2) But a trial court has discretion to deduct from a parent's monthly gross income the amount of straight line depreciation allowed by the Internal Revenue Code. [*Lawrence v. Tise*, 107 N.C.App. 140, 419 S.E.2d 176 (1992); see also *Holland v. Holland*, 169 N.C.App. 564, 610 S.E.2d 231 (2005) (trial court erred in treating all of father's farm equipment depreciation as nondeductible accelerated depreciation and by failing to exercise its discretion to deduct from father's gross income straight line depreciation allowed by Internal Revenue Code).]

(3) In the context of businesses involving the rental of real property, ordinary and necessary business expenses generally include expenses for repairs, property management and leasing fees, real estate taxes, insurance, and mortgage interest. Payments on the principal amount of a mortgage loan are not considered ordinary and necessary business expenses. [*Lawrence v. Tise*, 107 N.C.App. 140, 419 S.E.2d 176 (1992).]

(4) A court may refuse to allow a parent to deduct business expenses for a home office or personal vehicle, bad debts, depreciation, and repayment of the principal on a business loan if it determines that the expenses are not appropriate for the purpose of

determining gross income under the guidelines. [*Cauble v. Cauble*, 133 N.C.App. 390, 515 S.E.2d 708 (1999) (no error when court disallowed bad debt and depreciation expenses claimed by Subchapter C corp.); *Kennedy v. Kennedy*, 107 N.C.App. 695, 421 S.E.2d 795 (1992) (no error when court disallowed expenses for utilities, phone, truck lease, insurance, home and truck maintenance, and personal property taxes claimed by self-employed musician/father); *Lawrence v. Tise*, 107 N.C.App. 140, 419 S.E.2d 176 (1992) (no deduction for payments on mortgage principal secured by rental property). *Cf. Dillon v. Rains*, 193 N.C. App. 208, 666 S.E.2d 800 (2008)(while trial court has discretion to determine whether expenses should be deducted, trial court must make findings to show consideration of evidence presented concerning business expenses)]

7. Income received on an irregular, non-recurring or one-time basis.
 - a) When income is received on an irregular, nonrecurring, or one-time basis, the court may average or prorate the income over a specific period of time or require the parent to pay as child support the same percentage of the parent's nonrecurring income as that paid with respect to the parent's recurring income. [2006 and 2011 Guidelines. *But cf. Glass v. Glass*, 131 N.C. App. 784, 509 S.E.2d 236 (1998)(error for trial court to include income from bonuses obligor earned in the past several years where trial court made finding that obligor would not receive those bonuses for at least the next three years following the hearing).]
 - b) A one-time lump sum workers' compensation payment paid to the father was income. [*Freeze v. Freeze, unpublished opinion*, 159 N.C.App. 228, 582 S.E.2d 725 (2003)(trial court erred by failing to include a lump sum workers' compensation settlement as income attributable to father).]
 - c) Lump sum accident settlement placed in a family trust was "non-recurring income" within the meaning of the Guidelines. [*Spicer v. Spicer*, 168 N.C.App. 283, 607 S.E.2d 678 (2005) (no error in treating entire trust principal as non-recurring income under the Guidelines, rejecting father's argument that only the interest income generated by the trust should be considered).]
8. Income verification.
 - a) A parent's testimony or affidavit with respect to current income should be verified through appropriate documentation (pay stubs for the prior month, employer statements, or business receipts and expenses). Documentation of current income must be supplemented by providing a copy of the parent's most recent tax return to provide verification of earnings over a longer period. [2006 and 2011 Guidelines]

- b) In a IV-D or non-IV-D child support case, a written statement (or an employment verification form generated by the IV-D ACTS system) signed by the employer of a parent who is obligated to pay child support is admissible in a proceeding to establish, modify or enforce a child support order to prove the amount of the obligor's gross income. [G.S. § 110-139(c1)]
- c) A court may impose sanctions against a parent who fails to provide suitable documentation of the parent's income. [2006 and 2011 Guidelines]
- d) Father's stipulation that he would not raise inability to pay child support as defense did not relieve him from full disclosure of his financial condition. [*Shaw v. Cameron*, 125 N.C.App. 522, 481 S.E.2d 365 (1997) (error for trial court to limit the scope of discoverable information; to determine father's child support obligation under guidelines, mother was entitled to discover value and nature of father's interest in any partnerships or corporations and terms of any trust of which he might be beneficiary, as well as amount of related income).]

C. Imputed income – use of earning capacity.

1. The general rule is that a parent's child support obligation is determined by that parent's **actual** income at the time the award is made. [*State ex. rel. Godwin v. Williams*, 163 N.C. App. 353, 593 S.E.2d 123 (2004); *Hodge v. Hodge*, 147 N.C. App. 478, 556 S.E.2d 7 (2002).]
2. But one's **capacity to earn** may be used instead:
 - a) Where the parent is voluntarily unemployed or underemployed to such an extent that the parent cannot provide a minimum level of support for himself or herself and his or her children when the parent is physically and mentally capable of doing so; **and**
 - b) The parent's unemployment or underemployment is due to the parent's bad faith or deliberate suppression of income to avoid or minimize the parent's child support obligation. [2006 and 2011 Guidelines]
3. An intentional reduction in income, without more, is not sufficient to impute income. Some type of "bad faith" is required. [*See Pataky v. Pataky*, 160 N.C.App. 289, 585 S.E.2d 404 (2003), *aff'd in part, review dismissed in part*, 359 N.C. 65, 602 S.E.2d 360 (2004) (per curiam) (before earning capacity may be used as the basis of an award, there must be a showing that actions which reduced the party's income were taken in bad faith, to avoid family responsibilities); (*Kowalick v. Kowalick*, 129 N.C.App. 781, 501 S.E.2d 671 (1998) (before considering a party's earning capacity, trial court must make a finding that the party deliberately depressed its income in bad faith or otherwise disregarded its

child support obligation); *Sharpe v. Nobles*, 127 N.C.App. 705, 493 S.E.2d 288 (1997) (before using the earnings capacity rule there must be a showing that the actions which reduced a party's income were not taken in good faith).]

a) "Bad faith" has been recognized as a general term given to situations that trigger the earning capacity rule. Whether or not "bad faith" is the term used, it is clear that an intentional reduction in income is not sufficient to support the use of earning capacity rather than actual income unless it is proven to have been made to avoid a child support obligation. [*Cook v. Cook*, 159 N.C.App. 657, 583 S.E.2d 696 (2003).]

b) To base an award on earning capacity, the finder of fact must have before it sufficient evidence of the proscribed intent, which being a mental attitude, must ordinarily be proven by circumstantial evidence. [*Roberts v. McAllister*, 174 N.C. App. 369, 621 S.E.2d 191 (2005).]

c) A determination of bad faith in conjunction with suppression of income is best made on a case-by-case basis. [*Id.*; *Pataky v. Pataky*, 160 N.C. App. 289, 585 S.E.2d 404 (2003).]

4. Determining the amount of imputed income. The amount of potential income imputed to a parent must be based on the parent's employment potential and probable earnings level considering the parent's recent work history, occupational qualifications and prevailing job opportunities and earnings levels in the community. If the parent has no recent work history or vocational training, the amount imputed should not be less than the minimum wage for a forty hour week. [2006 and 2011 Guidelines]

5. Cases imputing income.

a) Income from position from which father was terminated imputed to him; court found father voluntarily unemployed because his actions at work irritated and embarrassed his employer resulting in an "entirely predictable termination." [*Wolf v. Wolf*, 151 N.C.App. 523, 566 S.E.2d 516 (2002).]

b) No error in imputing income to able-bodied 52 year old father who retired after current wife won a lottery; father voluntarily depressed his income in deliberate disregard of support obligation. [*Mason v. Erwin*, 157 N.C.App. 284, 579 S.E.2d 120 (2003).]

c) No error in imputing income to mother when she voluntarily and in bad faith stopped working as a real estate agent. [*King v. King*, 153 N.C.App. 181, 568 S.E.2d 864 (2002) (her explanation for not working, that time involved in trial of child support matter interfered with her ability to work, rejected by court).]

d) No error to imput income to mother who continued to be a stay-at-home mother evidencing a "naïve indifference" to the financial needs of her children born during her first marriage. [*Roberts v. McAllister*, 174

N.C. App. 369, 621 S.E.2d 191 (2005). *See also Thomas v. Thomas, unpublished*, 683 S.E.2d 791 (N.C. App., 2010); *Tardani v. Tardani, unpublished*, 689 S.E.2d 601 (2010)(father acted in bad faith by taking job as manager trainee at low wage when he had significant experience as a manager).]

6. Cases not imputing income.

a) Defendant who voluntarily resigned from his job to return to graduate school did not act in bad faith; earnings from former job not imputed to him. [*Pataky v. Pataky*, 160 N.C.App. 289, 585 S.E.2d 404 (2003), *aff'd in part, review dismissed in part*, 359 N.C. 65, 602 S.E.2d 360 (2004) (per curiam).]

b) Error for trial court to impute earnings to father merely because he resigned from his employment; court found resignation was not in bad faith. [*Cook v. Cook*, 159 N.C.App. 657, 583 S.E.2d 696 (2003).]

c) Error for trial court to impute income to father from investment account after father restructured his portfolio from holdings that produced more income to holdings that would favor long term growth; finding that father deliberately reduced his income, but did not do so in bad faith, not sufficient to justify application of earning capacity rule. [*Cook v. Cook*, 159 N.C.App. 657, 583 S.E.2d 696 (2003).]

d) Father's failure to look for work that would pay him what he made before his position was eliminated was not deliberate suppression of income or other bad faith action; his former "earning capacity" could not be used to impute income to him. [*Sharpe v. Nobles*, 127 N.C.App. 705, 493 S.E.2d 288 (1997).]

7. A trial court must make sufficient findings to justify applying the earning capacity rule.

a) If a parent is voluntarily unemployed or underemployed. . .and the court finds that the parent's voluntary unemployment or underemployment is the result of a parent's bad faith or deliberate suppression of income to avoid or minimize his or her child support obligation, child support may be calculated based on the parent's potential, rather than actual, income. [2006 and 2011 Guidelines]

b) Trial court made no findings as to defendant's present earnings, or as to defendant's reduction of income in bad faith; order that imputed income reversed. [*Ford v. Wright*, 170 N.C. App. 89, 611 S.E.2d 456 (2005).]

c) Trial court's order lacked any finding or conclusion that defendant depressed his income in bad faith; order for support based on earning capacity reversed. [*State ex. rel. Godwin v. Williams*, 163 N.C.App. 353, 593 S.E.2d 123 (2004) (error to impute income to full-time college student

at the minimum wage of \$5.15 per hour, on a full-time basis, without findings as to deliberate or bad faith conduct by defendant to suppress his income or otherwise avoid his child support obligation).]

d) Findings that husband's unemployment was voluntary and that he had acted in "bad faith" based on a conscious and reckless disregard of his duty to provide court-ordered child support sufficient to impute income to father. [*Wolf v. Wolf*, 151 N.C.App. 523, 566 S.E.2d 516 (2002) (noting trial court's "extensive findings of fact" outlining circumstances of father's termination).]

e) Error for trial court to calculate child support based on each party's "earning capacity"; order did not include any findings as to whether either party deliberately suppressed his or her income to avoid his or her support obligation. [*Bowers v. Bowers*, 141 N.C.App. 729, 541 S.E.2d 508 (2001).]

f) Trial court erred in imputing any amount of income to self-employed musician/father; no evidence in the record to support a finding that father deliberately depressed his income. [*Kennedy v. Kennedy*, 107 N.C.App. 695 (1992), 421 S.E.2d 795 (1992).]

8. Potential income may not be imputed to a parent who is physically or mentally incapacitated or who is caring for a child who is under the age of three years for whom child support is being determined. [2006 and 2011 Guidelines]