

Income tax marriage penalty now hits same-sex spouses too

Edith Windsor, the plaintiff in the landmark Supreme Court case declaring the Defense of Marriage Act unconstitutional, sued because the government's refusal to recognize her marriage led to an estate tax bill that an opposite-sex couple would not have faced.

From a tax perspective, the Supreme Court's decision in the Windsor case is certainly good news for the lucky 0.2 percent of decedents who pay federal estate tax. But income taxes are the key taxes that the rest of us pay. The news is not all good for same-sex couples whose marriages are now recognized by the federal government for income tax purposes.

Whether a marriage penalty or bonus applies generally depends on how similar the parties' incomes are. A bonus is typical for those with disparate incomes.

In a little-noticed report issued Sept. 9, the Congressional Research Service explored the federal tax implications of same-sex marriage, noting a previous government study's estimate that federal recognition of same-sex marriage could increase income tax revenue by \$200 million to \$400 million per year. The potential increase stems in part from an artifact of the design of our progressive tax system known as the marriage penalty.

As income increases, the rate of taxation also increases. However, the income thresholds at which increased rates apply do not move in tandem for single and married individuals. In other words, when two individuals marry, a greater (or lesser) portion of their combined income can fall into a higher tax bracket because of the thresholds at which the brackets apply.



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Whether a marriage penalty or bonus applies generally depends on how similar the parties' incomes are. A marriage penalty is typical for couples with similar incomes, and a marriage bonus is typical for couples with disparate incomes.

The CRS report provides an example of two partners earning \$100,000 each. If they were to marry, they would pay an \$879 marriage penalty. In contrast, if one partner earned \$50,000 and the other \$150,000, the couple would receive a \$557 marriage bonus. So the effect of federal recognition of same-sex marriage on tax revenue depends on the distribution of earnings between the spouses in these marriages.

A host of other factors will be important as well. Income tax credits that benefit taxpayers with children are now available to same-sex married couples. Previously, one partner would have had to claim each child as a dependent.

In addition, the recognition of same-sex marriage changes the rules for non-taxable employee compensation. Previously, employer contributions for health insurance covering the same-sex spouses of employees were taxable to those spouses, but the demise of DOMA changes this.

In all, the Government Accountability Office has estimated, there are 198 sections of the Internal Revenue Code in which marital status is a factor in determining benefits. Because of the many factors involved, the tax impact of marriage for individual couples will vary widely. Thus, computations of the tax impact of same-sex marriage also vary widely, with some commen-

tators predicting a revenue boost that is an order of magnitude less than the estimate of \$200 million to \$400 million.

Beginning with 2013, same-sex couples who are married in any domestic or foreign jurisdiction that recognizes their marriage must file as married for federal tax purposes, regardless of where they reside.

Other than divorce, there is no way to plan around the marriage penalty.

However, on Aug. 29, the IRS issued guidance stating that same-sex married couples who were previously required to file as single may choose to amend their tax returns and file as married for all open tax years. For most taxpayers, amended returns can be filed for 2010, 2011 and 2012.

Because filing amended returns is optional, same-sex married couples have the opportunity to choose the filing status that results in the greatest benefit for them.

The guidance does not address whether taxpayers filing amended returns for reasons other than changing their filing status are required to file as married. Taxpayers amending returns for other reasons should proceed with caution.

Because of the complexity of the computation, the only way to determine whether a penalty or bonus applies is to prepare pro forma returns. However, the Tax Policy Center has a calculator on its website, www.taxpolicycenter.org, that prepares back-of-the-envelope computations that may help couples determine whether preparing pro forma returns is worth the bother.

Most people marry for love, not money, but for the Treasury, federal recognition of same-sex marriage has a substantial monetary value. For the last three years, however, there is an unusual opportunity for same-sex couples to elect the tax treatment that minimizes their total tax, which—despite the patriotic benefits of voluntary contributions to the Treasury—should not be ignored.

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