



equal tax treatment for same-sex couples in the wake of recent supreme court ruling and irs guidance

MSK Client Alert

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Same-sex marriages now are being recognized under federal tax law for the first time. In June 2013, the Supreme Court released its decision in *United States v. Windsor*, 530 U.S. 12 (2013), declaring Section 3 of the federal Defense of Marriage Act (DOMA) unconstitutional. In Revenue Ruling 2013-17, the IRS detailed the tax-law consequences of the federal government's new recognition of same-sex marriages. This update describes the details of the IRS's ruling and reviews opportunities it presents for significant tax savings for high-net-worth same-sex married couples.

Previously, the federal government did not recognize same-sex marriages, even when those couples were legally married under state law, so opposite-sex couples enjoyed certain income- and estate-tax benefits denied to same-sex couples. Under the new law, however, marriage is marriage, and same-sex couples can now enjoy several significant advantages considered integral to opposite-sex tax planning for years.

Same-sex married couples should consider and review the following issues with their estate and income tax advisors:

- **Marital Deduction.** Same-sex couples can now take advantage of the gift- and estate-tax marital deduction. This allows spouses to give unlimited assets to each other, during life or at death, without gift tax or estate tax. At the death of the first spouse, assets can be passed to the surviving spouse, free of estate tax, deferring estate tax until the second death. Previously, the amount same-sex couples could leave to each other free of estate tax was limited to the lifetime exemption amount (\$5,340,000 this year).

Nuance: Trusts for the benefit of the surviving spouse must be drafted specifically to take advantage of this; it is not automatic. Because the marital deduction previously did not apply to same-sex couples, many trusts are drafted without the

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technical language to achieve the tax deferral. Now that tax deferral is possible, it is critical that same-sex married couples revisit their estate plans if they desire to pass assets to each other in trust, so that the technical language can be added.

- **Estate Tax Exemption Portability.** One of the newest estate-planning techniques introduced in 2010, portability allows a surviving spouse to use any portion of a deceased spouse's federal estate-tax-exemption amount not used by the deceased spouse. This is a great benefit where there is a disparity in net worth and the first spouse to die doesn't need his or her exemption, but the surviving spouse could use the extra exemption to shelter more of his or her larger estate.
- **Income Tax Returns.** Legally married same-sex couples must now file their income tax returns either "jointly" or as "married filing separately." In some instances (predominantly with two spouses who earn roughly the same annual income), this may result in same-sex married couples being subjected to the "marriage penalty" of increased brackets. If earnings are disproportionate, however, the couple may experience a lower overall rate from filing as a married couple.
- **Retirement Plans.** The surviving spouse of a same-sex couple can now take advantage of the beneficial rules allowing surviving spouses to roll over the deceased spouse's retirement account into a new or existing account in the surviving spouse's name.
- **Ability to Amend Prior Returns.** Same-sex couples may, but are not required to, file amended income tax returns for prior years if the statute of limitations is still open. This period is generally three years after the date the return was due, but may be longer in some circumstances. This could allow a couple who has a lower overall income-tax rate filing as "married" to apply that lower rate to prior years. It could also allow a surviving spouse to retroactively apply for a refund if the deceased spouse's estate paid estate tax at death, in a prior year, and the estate-tax marital deduction would have applied to amounts left to the surviving spouse. In fact, this is exactly what happened in *United States v. Windsor*.

Importantly, you do not need to live in a state that recognizes same-sex marriage to receive the tax benefits. The new federal law applies regardless of where a couple resides, so long as the marriage is valid under the laws of the state where the couple was married. For example, a same-sex couple legally married in California (which recognizes same-sex marriages), who then moved to Texas (which does not recognize same-sex marriages), will be treated as married for all federal tax purposes.

However, the new law and tax benefits do not apply to registered domestic partnerships, civil unions, or other similar relationships. Couples currently in these types of unions may wish to weigh the benefits of getting married, as there are now serious tax benefits to doing so for high-net-worth couples who wish to leave their assets to each other.

Please contact any member of our Trust and Estates Practice Group if you have any questions regarding this development or how your estate plan could be affected.