

September 2013 Updates

Pratt & Kulsrud User:

Below are two recent developments that may liven up your classroom discussions this semester: a ruling on the treatment of same-sex marriages and a \$1.1 million assessment imposed on billionaire Sumner Redstone for failure to file a gift tax return 41 years ago (a hearty thanks to Jan Meade of the University of Houston for the note on Mr. Redstone). Also attached is a slide, reflecting the new ruling.

SAME-SEX MARRIAGES

On Thursday, August, 29, 2013, the IRS issued Rev. Rul. 2013-17, announcing that same-sex couples that were legally married in jurisdictions that recognize their marriages will be treated as married for federal tax purposes. Thus, if a same sex couple was legally married in a state that allows same sex marriage, the couple will be considered married for federal tax purposes even though the couple lives (is domiciled) in a state that does not recognize same sex marriages. Note that such couples may be married for federal tax purposes but may not be married for state income tax purposes. For example, if a same-sex couple was legally married in a state that recognizes same-sex marriage such as New York but lives in Indiana where same-sex marriage is not recognized, the couple may file a joint return for federal purposes but would be treated as two single individuals in Indiana.

The 15-page ruling will apply to all federal tax provisions where marriage is a factor. This includes not only the income tax but also the estate, gift and generation skipping transfer taxes. Tax provisions in which marriage is a factor, include filing status, personal and dependency exemptions, the standard deduction, employee benefits, contributions to IRAs, the earned income tax credit, the child tax credit, and many others. According to the ruling, there are more than 200 provisions in the Code and regulations that include the terms “spouse,” “marriage,” “husband,” “wife,” or “husband and wife.” According to the ruling, the IRS will treat gender-neutral terms, such as “spouse” and “marriage,” as including, respectively, an individual who is married to a person of the same sex if the couple is lawfully married under state law and such a marriage is between same-sex individuals. The terms “husband,” “wife,” and “husband and wife” will be interpreted to include same-sex spouses.

The ruling will apply to taxpayers who are in any same-sex marriage legally entered into in one of the 50 states, the District of Columbia, a U.S. territory, or a foreign country. As of August 2013, the following jurisdictions legally recognize same sex marriage: California, Connecticut, Delaware, Iowa, Maine, Maryland, Massachusetts, Minnesota, New Hampshire, New York, Rhode Island, Vermont, and Washington, the District of Columbia, several counties in New Mexico, and 5 Native American tribes. The Defense of Marriage Act (DOMA), enacted in 1996, allows states

to refuse to recognize same-sex marriages performed under the laws of other states. Section 3 of DOMA prevented the federal government from recognizing same-sex marriages until that provision was ruled unconstitutional by the U.S. Supreme Court on June 26, 2013, in *United States v. Windsor* 570 U.S. ____ (2013).

The ruling will not apply to taxpayers who are in registered domestic partnerships, civil unions, or similar formal relationships recognized under state law that do not have the status of legal marriage under state law.

Under the ruling, legally married same-sex couples generally will file their 2013 federal income tax returns using either “married filing jointly” or “married filing separately” filing status. Such individuals may, but are not required to file original or amended returns choosing to be treated as married for federal tax purposes for one or more prior tax years still open under the statute of limitations, if they were legally married during that tax year.

Note that in determining whether the state-of-domicile or state-of-ceremony approach should be used in determining marital status, Treasury selected the state-of-ceremony approach. Apparently, this approach was selected to prevent same-sex couples from gaming the system and selecting the state to live in based on the best tax consequences.

While the federal tax treatment for all legally married couples is now the same, this does not mean that the change is beneficial for all same sex-couples. Same-sex couples are now forced to file jointly or married-filing separately. They will now face the possibility of a marriage tax penalty. In addition, same-sex couples who must file as single individuals for state purposes face additional complexity. These individuals will need to make decisions about which spouse claims their various deductions and reports non-wage income.

FAILURE TO FILE A GIFT TAX RETURN

Beware! The statute of limitations never begins to run if a tax return is not filed. Billionaire Sumner Redstone, the chairman of Viacom Inc. and CBS Corp., received a note from the IRS last January that he owes \$1.1 million in taxes, penalties and interest for failure to file a gift tax return 41 years ago in 1972. The 89-year-old Redstone is worth \$4.9 billion, according to the Bloomberg Billionaires Index. He started his career on the other side of tax disputes as a lawyer for the U.S. Department of Justice.

Hope your semester is going well! If you have any questions regarding the Pratt & Kulsrud texts, please contact me.

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