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IRS Application of Income-Splitting to Same-Sex Couples

Answers to Some Frequently Asked Questions (FAQs)

January 26, 2012

The U.S. Internal Revenue Service (IRS) announced in May 2010 a change in its treatment of income earned by registered domestic partners (RDPs) in California. The IRS now will apply California's community property laws to California RDPs the same way—to reflect "income-splitting" for community property—that it long has applied those laws to different-sex married couples in California who file their federal income tax returns separately. The IRS also subsequently confirmed that this change will apply similarly to same-sex spouses in California and RDPs in Washington and Nevada. This represents a step in the direction of treating same-sex couples who have formalized their relationship under state law the same as married different-sex couples. The change is welcome progress towards our community's goal of full legal equality for same-sex couples, even though it makes preparation of tax returns more complicated for many couples during this period of change. In addition, although the change likely will result in higher income taxes for some same-sex couples, it is anticipated that many more couples will see a decrease in their income taxes.

The following questions and answers (Q&As) are intended to help same-sex couples and tax professionals understand the key components and importance of this change, but they are not comprehensive. Rather, they focus on some common questions, and also identify some aspects of the new IRS position and its implementation that remain unclear. This document is based upon information provided by the IRS, which has focused principally on California residents, with some recent clarifications concerning residents of Washington and Nevada. As the laws relating to the treatment of same-sex relationships continue to evolve, same-sex couples should expect more changes, including further clarifications from the IRS. As part of our public education efforts, Lambda Legal intends to issue further updates on these matters from time to time. Couples also may wish to consider the issues addressed in Lambda Legal's "Take the Power" life planning toolkit and other information available on the Lambda Legal website about steps lesbian, gay, bisexual and transgender (LGBT) people and those living with HIV may wish to take to protect their assets and their loved ones.

1. How did the IRS change its position on the federal income taxes of California RDPs?

In May 2010, the IRS issued a memorandum concluding that community property earned by California RDPs by operation of state law must be recognized as such when determining each California RDP's income for federal income tax purposes. As a result, the IRS now will treat community property earned by California RDPs the same way it long has treated community property earned by married different-sex couples in California who file separate federal tax returns, which is to add together all the community income earned by both members of the couple and to allocate half to each one's separate return. This is called "income-splitting." Accordingly, in most cases, one-half of community income earned by each California RDP similarly should be reported by the other RDP for federal income tax purposes.

This is a change from a prior IRS position. In 2006, the IRS announced that it would treat community income earned by each California RDP as fully taxable to that individual, despite the fact that community income is earned jointly by both RDPs by operation of California law. Lambda Legal has believed the prior IRS position was incorrect. It has been settled law for many decades that, for federal income tax purposes, state law determines ownership of property and federal law then determines how much federal tax the owner must pay. The U.S. Supreme Court has held that it is unconstitutional to require an individual to pay income tax on monies the individual does not own. The IRS position in 2006 appeared to be consistent with California's income tax treatment of RDPs' community property from 2003 through 2006. It has been clearly inconsistent since 2007.

Under its new approach, the IRS appropriately will apply California's community property principles to determine California RDPs' taxable income for federal tax purposes. As discussed in Q&A #13, the new IRS approach can be applied retroactively back to January 2007, when a change in California income tax law took effect. For a discussion of the tax periods to which the new IRS approach applies, see Q&As #12 and #13.

The effect of the new IRS position on the combined tax obligations of a same-sex couple in a California RDP will depend on the couple's particular situation. See Q&As #3 - #10. As a result, same-sex couples should consult with an attorney or tax professional with experience in this area of law about how the new IRS position may affect them.

2. What are "community income" and "separate income" under California law?

Community income: What constitutes community income may vary from state to state. Under California's community property laws, two individuals who have married or registered with the state as domestic partners are seen as having created a "community" of two when they formalized their status as a couple. They are presumed by law to acquire at least some of their income jointly as "community property," which is owned equally by both of them, unless they have taken specified steps to opt out of the community property system.

Under California law, "community income" generally is income from the following:

- Salaries, wages, or pay for services that either spouse or RDP, or both, received during the marriage or registered domestic partnership, for periods that the couple lives in California (or somewhere else that applies community property law to their relationship).
- Community property, which generally includes property that either spouse or RDP, or both, acquired with community funds during the marriage or registered domestic partnership while living in California. Community property generally includes all real estate so acquired, even if the real estate is located outside of California.

Separate income: In California, separate income is income from separate property, which generally includes the following:

- Property that either spouse or RDP owned separately before the marriage or domestic partnership registration.
- Money earned while living in a state that did not apply community property laws to the earnings.
- Property either spouse or RDP received as a gift or separate inheritance during the marriage or registered domestic partnership.
- Property bought with separate funds, or exchanged for separate property, during the marriage or registered domestic partnership.
- The part of property bought with separate funds, if part was bought with community funds and part with separate funds.

There are also certain types of income, such as social security, for which it is presently unclear whether they are community or separate income.

Conversion of "community" to "separate" (and vice-versa) by agreement: California RDPs, just like married different-sex couples in California, can enter into an agreement that affects the status of property or income as community or separate property. Such an agreement sometimes can result in a federal gift tax. See Q&A #8. Couples should consult with an attorney or tax professional with expertise in this area about whether such an agreement is sensible in their particular situation.

3. Does this new IRS position mean a same-sex couple can file their federal income taxes in a joint return like married heterosexual couples?

No. At present, neither RDPs nor married same-sex couples can file a joint federal income tax return. Under current IRS rules and the federal so-called "Defense of Marriage Act," RDPs and same-sex spouses must continue to file separate federal income tax returns as "single" or, if applicable, as "head of household." The new IRS position could, however, prevent one member of the same-sex RDP couple from filing as "head of household," because the "income-splitting" might prevent that member from claiming the other RDP as a dependent. See Q&A #6.

4. How does "income-splitting" under this new IRS position affect the amount of income each California RDP reports on his or her federal income tax return?

Under the old IRS position, California RDPs' community property was not recognized as community property for federal income tax purposes. Rather, under the old approach, each RDP was required to report the full amount of his or her individual income notwithstanding that those funds actually were half-owned by his or her registered partner.

Under the new IRS approach of recognizing the actual ownership of California RDPs' income as determined by the state's community property laws, each RDP reports one-half of the community income that is earned by either RDP. Hence, as noted above in Q&A #1, this community property treatment is sometimes referred to as "income-splitting." But it is important to note that, under the new IRS approach, each RDP continues to report the *full* amount of his or her *separate* income.

Reporting income from wages under the new IRS position:

As an example of the treatment of wages under the new IRS position, consider Kyle and Freddie, who are California RDPs. Kyle is a graduate student earning $10,000 a year, while Freddie is an accountant earning $90,000 a year. Under the old IRS position, Freddie and Kyle would each have to file a federal tax return, Freddie would report all $90,000 of his earned income in his return, and Kyle would report only his $10,000 in his return.

Under the new IRS position, however, the community property character of the couple's respective wages, as established by California law, is recognized. That means the couple's community income is owned equally and should be split equally for federal income tax reporting purposes. Therefore, although Freddie and Kyle will still file separate returns, each will report an income of $50,000 – one-half of their total community income of $100,000 (Freddie's $90,000 plus Kyle's $10,000).

This change can be significant. Although they still report a combined $100,000 of income, Freddie and Kyle's overall tax burden should be lower. Because income tax rates generally increase as an individual earns more, the combined taxes on two incomes of $50,000 each may be less than the combined taxes on one income of $10,000 and one income of $90,000.

If Kyle and Freddie earned comparable salaries (or, if each would be in the top federal tax bracket under both the old and new IRS position regarding the community income of California RDPs), this change in IRS approach probably would make less of a difference to their combined income tax liability. If Freddie or Kyle were subject to the Alternative Minimum Tax ("AMT"), that also could affect the extent to which they benefit from the new approach.

Reporting income from a business or investment under the new IRS position:

The change in IRS position does *not* affect—and "income-splitting" does not apply to—the tax treatment of *separate* (rather than *community*) income. For example, if Kyle owns certain investments as his separate property, he still reports *all* the income from those separate property investments himself. Freddie reports none of that income on his federal tax return. Income from investments that either Freddie or Kyle hold as community property, however, should be split evenly between Kyle and Freddie's two separate tax returns in the same way as their income from wages.

As an example of the treatment of business income and expenses under the new IRS position, consider Dan and Steve, who are California RDPs. Dan is the sole proprietor of a garden nursery which is community property. In one year, the nursery incurred $22,000 in cost of goods sold and $24,000 in rent and other business expenses. That same year, the nursery had gross receipts of $120,000.

Because the nursery expenses and revenue arise out of a trade or business that is their community property, if the new IRS position is applied to the year in question, Dan and Steve would split those amounts evenly between their respective separate federal tax returns. As a result, Dan and Steve each would report $60,000 in revenue as well as $12,000 of rent and other expenses, and $11,000 of cost of goods sold, most likely on their respective Schedules C on their federal tax returns.

For a discussion about who is responsible for self-employment taxes related to the nursery business, see Q&A #5.

Exceptions to "income-splitting" community property treatment under the new IRS position:

Under the new IRS position, federal tax law now clearly respects California RDPs' state law community property rights to the same extent it has long respected the state law community property rights of different-sex spouses. In certain respects, however, state community property laws still *do not* affect federal tax treatment, even for different-sex spouses. For more details, see Q&A #5.

5. Does this new IRS position change all amounts that California RDPs report as income, deductions, or penalties?

No. *Separate* (in other words, non-*community*) income described in Q&A #2, and associated deductions and penalties, are all unaffected. Under the new IRS position, each California RDP must continue to report the full amount of his or her separate income on his or her federal income tax return.

In addition, as discussed further in Q&A #11 below, the IRS has suggested that same-sex RDPs covered by the new IRS position should follow its guidelines for different-sex spouses filing separate federal tax returns, set out in IRS Publication 555,[1] when preparing the separate federal tax returns for each RDP. As described in IRS Publication 555 and other IRS authority, income, deductions, and penalties associated with particular items are always treated as separate under federal tax law, even for different-sex spouses in community property states.[2] Such items include:

- Individual retirement arrangements, including Individual Retirement Accounts (IRAs), SEP-IRAs, SIMPLE IRAs, and Roth IRAs. Whether distributions from a 401(k) plan are treated as separate or community property is a complex question. The answer may depend in part, on the extent to which contributions to the plan were made from separate or community property. Because of that complexity, as well as some potentially conflicting authority in the area, RDPs should consult with a tax professional about their individual situations regarding the appropriate treatment of 401(k) plan matters.
- All or part of the distributions from a pension plan. The extent to which federal tax law treats a pension plan as separate property, community property or both separate and community property (in part) may depend on the particular facts and circumstances.
- Coverdell Education Savings Accounts (ESAs).
- FICA (Social Security and Medicare withholding).
- Estimated tax payments. For taxable income that is *not* subject to withholding, each individual RDP may need to make his or her own separate estimated federal tax payments to cover federal taxes on his or her share of all community income plus their own separate income.

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[1] IRS Publication 555 is available at www.irs.gov/pub/irs-pdf/p555.pdf.

[2] Although federal tax law generally defers to state law when federal law does not itself identify which taxpayers are to include which amounts on their returns, federal tax law sometimes specifies whether community property laws apply.

Note, however, that the IRS has indicated in Publication 555 that RDPs and same-sex spouses in California should report community income for self-employment tax purposes the same way they do for income tax purposes. Thus, applying this rule to the example in Q&A #4, Dan and Steve would each be responsible for half of the self-employment taxes related to the nursery business, even though Dan carried on the business. Same-sex couples should consult with a tax professional with expertise in this area about the applicability of this rule to their individual situations.

Depending on your personal situation, you might have additional items that are always treated as separate for federal tax purposes.

6. Are a California RDP's tax exemptions affected by this new IRS position?

A California RDP's tax exemptions could be affected. For example, when one RDP earns little income, he or she can sometimes be claimed as a dependent by his or her RDP, which usually means an additional exemption for the taxpaying RDP. Community property law can change the amount of income each RDP is recognized as earning, however. That may affect whether the primary wage-earner in the RDP couple can claim the no- or very low-wage-earning partner as a dependent.

Consider Susan and Laura, who are California RDPs. In one year, Susan has $100,000 in wages, and Laura has only $1,000 of investment income. Under the old IRS position, which didn't treat Susan's wages as community income, Laura's income probably would have been low enough to permit her (if she also met other requirements) to qualify as Susan's dependent for U.S. tax purposes. Under the new IRS position recognizing Susan's wages as community income, however, Laura is treated as owning $50,000 of Susan's wages – which probably would prevent Susan from claiming Laura as a dependent.

7. Are a California RDP's tax deductions affected by this new IRS position?

Yes. When California RDPs incur expenses to earn or produce community income, each RDP may deduct one-half of such expenses on his or her federal income tax return. Expenses incurred to earn or produce separate income, however, are deductible only by the RDP who earns that separate income. And, as discussed in Q&A #5, each RDP reports the full amount of his or her separate income on his or her federal income tax return.

The treatment of deductions for charitable contributions depends on the source of the funds or other assets used to make the contribution. If separate property is contributed, the deduction should be taken only by the RDP whose separate property was used. If community property is contributed, the deduction should be split between both RDPs. As noted in Q&A #5, however, deductions for IRA contributions and certain other items (even if made from community property) cannot be split between RDPs or spouses.

8. Can California RDPs opt out of community property treatment?

Yes. California RDPs, just like different-sex married couples in California, can enter into an agreement that affects the "community" or "separate" status of property or income. For example, such an agreement between RDPs could be used to convert certain property from separate to community property or vice-versa.

Such an agreement, however, must generally satisfy various requirements, such as the requirement that it be in writing. It could also possibly be treated as a taxable gift for purposes of federal gift tax if the agreement converts property that already exists (as opposed to future community property that has yet to be earned). Same-sex couples should consult with an attorney or tax professional with relevant expertise about the advisability of such an agreement in their particular situation.

If California RDPs have *not* opted out of community property treatment through such an agreement, they must apply community property laws when completing their federal tax returns for tax year 2010 and after. For more details on the tax periods covered by the new IRS position, see Q&As #12 and #13.

9. How does this new IRS position affect what happens with the income taxes withheld from a California RDP's paycheck?

When a California RDP's wages are community income, each RDP should report one-half of the credit from the income tax withheld. If California RDPs have entered into an agreement to opt out of community property treatment, however, the treatment of withholdings would be different. See Q&A #8.

For example, Sally and Lisa are California RDPs with no dependents, and their only source of income is their wages, which are community income. In one tax year, Sally has $80,000 in wages and had $16,000 of income tax withheld from those wages. In the same year Laura has $180,000 in wages and $45,000 of income tax withheld. Unless they have opted out of community property treatment, Sally and Lisa should each report $130,000 in wages and take a credit for $30,500 of income tax withheld.

Both Sally and Lisa could be owed a refund, if they have not had their employers adjust the amount of federal income tax withheld to reflect the way community property law affects ownership of their income and the corresponding deductions.[3]

[3] To determine the amount of federal income tax to withhold, employers collect information from their employees on IRS Form W-4. There are various methods for determining what information to provide. Same-sex couples should consult with a tax professional about their individual situations.

In our example, Sally and Lisa would be in different tax brackets if they were not subject to community property laws. So, relative to their individual tax liabilities based on community property treatment, "too much" would be withheld from Lisa's wages but "too little" would be withheld from Sally's wages. Moreover, the amount over-withheld from Lisa would be larger than the amount under-withheld from Sally, because Lisa's income would be withheld at a higher tax rate than Sally's income. Just as they would split their aggregate wages and aggregate withholdings equally when filing their separate federal tax returns, Sally and Lisa would also split equally the net total amount over-withheld. Both of them could therefore be entitled to receive a refund.

As noted in Q&A #4, however, the Alternative Minimum Tax (or "AMT") may also affect any net benefit to Sally and Lisa, including whether either or both of them would be owed a refund in our example above, due to the new IRS approach to California RDPs' community income.

10. Does this new IRS position mean that one RDP will owe federal gift taxes on community income earned by the other RDP?

No. Because community property allocation of income and expenses operates by law, there is no taxable transfer of assets between the RDPs. Thus, for federal tax purposes, the allocation of community property income and expenses to reflect actual shared ownership should *not* be treated as a gift from one RDP to the other. If two spouses or RDPs agree to convert certain property from separate to community property or vice-versa, however, such a conversion *may* result in a federal gift tax. See Q&A #8.

11. Is there any IRS guidance on how same-sex RDPs should complete their separate federal income tax returns under the new IRS position?

The IRS has suggested that, when applying the new IRS position to their separate tax returns, California RDPs should follow the guidance provided in IRS Publication 555 for married different-sex taxpayers filing separately.[4]

It is important to note, however, that some of the advice in IRS Publication 555 is based on the federal filing status of "married filing separately," *not* community property law.[5] Such advice about the "married filing separately" status currently does *not* apply to California RDPs, because California RDPs are not yet authorized to use that filing status. (Likewise, California RDPs have not yet been authorized to file as "married filing jointly." See Q&A #3.) In addition to reviewing IRS Publication 555, RDPs filing tax returns as directed by the new IRS position should consult their tax professionals about their particular situation. Neither these Q&As nor IRS Publication 555 can substitute for individualized advice about how this new IRS position affects you, or about how you should file your own federal tax returns.

12. When is this new IRS position effective?

The IRS has instructed that income-splitting will be mandatory beginning with income earned in 2010.[6] This means that tax returns beginning with those filed in 2011 generally must follow the new IRS position.

Please note that this new instruction differs from the language of the May 2010 IRS memorandum, which seemed to suggest that taxpayers would have the choice of electing to follow either the new IRS position or the old IRS position. The IRS's new instructions now state that taxpayers generally do not have such a choice with respect to income earned in 2010.

13. Is this new IRS position retroactive?

Yes, for certain prior tax periods *if the taxpayer chooses*. California began to recognize RDPs' community property for *state* income tax purposes starting on January 1, 2007. The IRS accordingly stated that it would allow California RDPs to amend their federal tax returns (or, if they haven't filed, to file a late tax return) for calendar years 2007, 2008, and 2009 in order to reflect the partners' ownership of community property, although this is generally subject to a three-year time limit from the date a return was due. (For Washington and Nevada, see Q&A #16 & #17). It is important for RDPs to consult with a knowledgeable attorney or tax professional to determine what deadlines might apply in their particular circumstances. Because the IRS has instructed that income-splitting was mandatory for income earned in 2010, RDPs who did not apply income-splitting to their tax returns filed in 2011 may also wish to amend those tax returns.

To apply the new IRS position to a prior tax period, a same-sex couple must have been RDPs when the income, gain or loss occurred. It appears that a same-sex couple who chooses to amend (or to late-file) their respective federal tax returns for a prior tax period solely to apply the new IRS position should *not* be subject to penalties if their prior filing was in compliance with the guidance provided by the IRS at the earlier time. But those taxpayers may owe statutory interest on any late tax

[4] Note again that IRS Publication 555 is available at www.irs.gov/pub/irs-pdf/p555.pdf.

[5] For example, IRS Publication 555 states that when a couple files "married filing separately," each person must claim his or her own exemption amount for that year. This is due to their 'married filing separately" filing status, rather than their ownership of community property.

[6] The IRS has stated that "A RDP in Nevada, Washington, or California (or a person in California who is married to a person of the same sex) generally must report half the combined community income earned by the individual and his or her domestic partner (or same-sex spouse)." Publication 555 (2010).

payments in connection with the amendment (or late filing) of federal tax returns for those prior periods.[7]

Those taxpayers may also owe what is described as a "penalty" for failing to pay timely estimated taxes. For 2007-2009, a taxpayer might owe this penalty only if she or he did not previously file a federal income tax return for the year at issue. Taxpayers who amend a previously filed return, even if that previously filed return showed zero (0) tax owed, should not be subject to this penalty.[8]

Likewise, any such taxpayer entitled to a federal tax refund as a result of the amended return may receive some interest on the amount refunded. The combined effect on a same-sex couple of amending (or late-filing) their separate tax returns for prior tax periods in order to apply the new IRS position will depend on the couple's particular situation. If the refund (including interest) to which one RDP would be entitled is greater than the corresponding tax, interest, and penalty for the other, and the difference more than covers the related attorney's or tax professional's fees, then filing amended returns may well be a sensible step.

Finally, the amendment or late-filing of a tax return for a prior tax period may extend the statute of limitations on tax obligations for such period, or have other important consequences separate from the implications of the new IRS position confirming recognition of RDPs' community property. So, again, RDPs should consult their attorney or tax professional about the advisability, in their particular situation, of applying the new IRS position retroactively.[9]

14. How will this new IRS position affect California married same-sex couples who are not also California RDPs?

The IRS has stated that its new position will apply equally to both California married same-sex couples and California RDPs: "A RDP in . . . California (or a person in California who is married to a person of the same sex) generally must report half the combined community income earned by the individual and his or her domestic partner (or same-sex spouse)." *See* Publication 555 (2010).

As noted in Q&A #1, the new IRS position reflects long-standing federal law that the IRS generally must defer to state laws that determine who owns what property, and in particular, what comprises an individual's ownership of community property. Thus, the new IRS position applies to *any* same-sex couple subject to California community property law. Under California law, this would include any same-sex couple in California who:

- married *before* November 5, 2008 (the date California's Proposition 8 took effect) in any country or state, including California, that at the time of the marriage permitted same-sex couples to marry,[10] or
- married *on or after* November 5, 2008 outside of California in any country or state, such as Canada or Massachusetts, that at the time of the marriage permitted same-sex couples to marry.[11]

There may be some confusion about whether the federal so-called "Defense of Marriage Act" (DOMA) requires an exception to the settled rule that state law determines ownership of property, such that the community property owned by a same-sex couple because they are married (rather than in an RDP) should not be recognized for federal income tax purposes. It does not. The IRS's change of position to recognize the community property owned by RDPs, despite the lack of any federal law acknowledging the existence and rights of RDPs, confirms that the IRS appreciates and intends to follow the settled rule that state law governs as to property ownership.[12]

15. How might this new IRS position affect same-sex couples outside of California?

This depends on state law where the couple lives. Only a minority of states now have community property, and in only a few of them could the new IRS position potentially apply because the states must both allow or recognize formalized relationships between same-sex couples *and* apply their community property laws to couples in such relationships.[13]

[7] For example, federal income taxes owed with respect to calendar year 2007 ordinarily would have been due by April 15, 2008. If payment were made by September 30, 2010, the interest rates would range from 4-6% per year.

[8] For additional information about this penalty, see IRS Publication 505 for the year at issue (available at www.irs.gov/pub/irs-pdf/p505.pdf for 2010 and 2009, www.irs.gov/pub/irs-prior/p505--2009.pdf for 2008, and www.irs.gov/pub/irs-prior/p505--2008.pdf for 2007).

[9] If you file federal tax returns for a prior tax period in order to apply the new IRS position regarding RDPs' community property and the IRS responds with any questions or objections to the proposed recognition of your community property for the prior period, you can Lambda Legal's Help Desk at (213) 382-7600 ext. 330 to let us know.

[10] Under California law, these marriages remain valid notwithstanding Proposition 8. See Cal. Family Code § 308(b); *In re Marriage Cases*, 183 P.3d 384 (2008).

[11] Under California law, these same-sex couples have the same legal rights and responsibilities (including community property treatment) as married couples with the exception of the designation of "marriage." See Cal. Family Code § 308(c).

[12] Again, if you are a California married same-sex couple who applies community property treatment to your separate federal tax returns and the IRS questions your doing so, you can contact Lambda Legal's Help Desk at (213) 382-7600 ext. 330 to let us know.

[13] In addition to California, Nevada, and Washington, the other states with community property laws are Alaska, Arizona, Idaho, Louisiana, New Mexico, Texas, and Wisconsin. Alaska and Wisconsin community property laws do not apply to the same-sex relationships that are recognized in those states. Indeed, it is notable that the IRS has not yet even stated whether it respects, for federal tax purposes, the

When a state applies its community property laws to same-sex couples in a manner similar to California's treatment of RDPs, it is reasonable to anticipate that the IRS will, or at least should, treat these taxpayers as it now will treat California RDPs.

At present, California, Nevada and Washington are the only states that *both* recognize same-sex relationships comprehensively under state law (e.g., with a broad form of domestic partnerships and/or marriage) *and* have community property, which applies to same-sex and different-sex couples alike after they formalize their relationship under state law.

So, same-sex couples in states other than California, Nevada, or Washington appear to be unaffected by the new IRS position, at least until their state satisfies both criteria. See Q&A #16 and #17 for a discussion of how the new IRS position will apply in Washington and Nevada.

Further, in some situations, whether and how the new IRS position is likely to apply might also depend on how the state itself applies its community property laws to same-sex couples. Among other things, when deciding whether and how its position on California RDPs should apply to same-sex couples in another state, the IRS might consider whether state law treats registered and/or married same-sex couples differently from different-sex married couples for state income tax purposes,[14] or whether the state has an income tax system at all.[15] Because application of the new IRS position may depend on future state laws, and because those laws may vary from state to state, those situations are difficult to analyze at this time. Nonetheless, the broad reasoning behind the new IRS position suggests that, if state law treats same-sex couples in legally-recognized relationships the same way it treats different-sex spouses with respect to acquisition and ownership of community property, then federal tax law should recognize and treat consistently those state-law property rights, regardless of which state family law rules caused the property rights to exist.

16. How will this new IRS position affect same-sex RDPs registered and living in Washington?

The IRS has stated that its new position will apply to Washington RDPs. Publication 555 (2010) provides that "A RDP in . . . Washington . . . generally must report half the combined community income earned by the individual and his or her domestic partner."As noted in Q&A #15, Washington law currently recognizes same-sex RDPs and applies community property treatment to couples in those relationships. For federal tax purposes, the IRS applies Washington community property laws to different-sex spouses living in that state.[16]

The IRS has not indicated whether income-splitting will apply to Washington RDPs retroactively. However, based on the approach taken in California, the new IRS position should apply to periods after June 12, 2008 (the date when Washington recognized community property ownership for RDPs).

To reduce uncertainty, Washington RDPs might consider asking the IRS for guidance on how the new IRS position applies to them retroactively. In addition, same-sex couples residing in the state of Washington who entered into a legal relationship (e.g., marriage or a limited domestic partnership) in a state other than Washington might consider registering as RDPs under Washington law.[17] Same-sex couples should, however, consider consulting their attorney or tax professional about the advisability of doing so given their particular situation. A sensible first step is to consider the issues addressed in Lambda Legal's toolkit, "Take the Power" (available at www.lambdalegal.org/publications/take-the-power/).[18]

"community property election" granted under Alaska state law for different-sex married couples in that state. The other community property states have yet to confirm by state statute or a court ruling that state law recognizes same-sex couples' relationships and/or applies the state's community property laws to such relationships. However, in New Mexico, the Attorney General issued an opinion that same-sex couples who marry out-of-state should be treated as spouses for state law purposes. N.M. Att'y Gen. Op. No. 11-01. Same-sex couples in New Mexico who married out-of-state should consider consulting their attorney or tax professional about how to report their income on their state and federal income tax returns.

[14] For example, in 2005 and 2006, when California generally applied community property law to its RDPs for most purposes except state income tax purposes, the IRS also refused to recognize RDPs' community income for federal income tax purposes. When the IRS addressed the issue in 2006, the agency took the position that income-splitting by RDPs would not be proper for federal tax purposes because the Supreme Court cases approving income-splitting only had addressed community property that existed as a consequence of marriage, and registered domestic partnerships are not marriages. The IRS explains its change of position as warranted because California now recognizes RDPs' community income for state income tax purposes as well as a range of other purposes, and seemingly has abandoned its prior view that community property can only exist for federal income tax purposes due to a marriage.

[15] It is notable that, for federal tax purposes, the IRS generally applies community property laws to different-sex spouses in states with community property even when the state does *not* impose a state income tax. As discussed in Q&A #16 and #17, this is the case in both Washington and Nevada.

[16] For different-sex spouses, the IRS recognizes the shared ownership of community income in Washington because of such property's ownership under state law, which is unrelated to the fact that Washington does not presently have a state income tax.

[17] Washington law treats any couple in a same-sex union, if that union was validly formed under the law of another jurisdiction and is substantially equivalent to a Washington registered domestic partnership. *See* RCW § 26.60.090 (2011).

[18] If you are a Washington RDP who applies community property treatment to your federal tax return and the IRS questions your doing so, you can contact Lambda Legal's Help Desk at (213) 382-7600 ext. 330 and alert us.

17. How will this new IRS position affect same-sex RDPs registered and living in Nevada?

The IRS has stated that its new position will apply to Nevada RDPs. Publication 555 (2010) provides that "A RDP in Nevada . . . generally must report half the combined community income earned by the individual and his or her domestic partner."

The IRS has not indicated whether income-splitting will apply to Nevada RDPs retroactively. However, based on the approach taken in California, the new IRS position should apply to periods after October 1, 2009 (the date when Nevada recognized community property ownership for RDPs). To reduce uncertainty, Nevada RDPs might consider asking the IRS for guidance on how the new IRS position applies to them retroactively.

Same-sex couples living in Nevada who entered into a legal relationship (e.g., civil union, marriage, or domestic partnership) in a state other than Nevada should note that they will not be treated as RDPs under Nevada law unless they register with the state of Nevada.[19] Before doing so, same-sex couples should consider consulting their attorney or tax professional about the advisability of taking that step given their individual situation. As a start, couples should consider the issues addressed in Lambda Legal's toolkit, "Take the Power" (available on Lambda Legal's website at www.lambdalegal.org/publications/take-the-power/).[20]

18. Will the new IRS position affect different-sex RDPs in California, Washington, and Nevada?

Yes. The new IRS position does not distinguish between same-sex versus different-sex RDPs. Thus, community property for both types of couples is subject to income-splitting.

In California and Washington, different-sex couples may register as domestic partners so long as at least one partner is 62 years of age or older and the other requirements of entering a domestic partnership are satisfied. In Nevada, both same-sex and different-sex couples may register as domestic partners as long as both partners are at least 18 years old, and so long as the other requirements of entering a domestic partnership are satisfied.

19. Will this new IRS position affect the receipt of means-tested public benefits?

It is possible that the new IRS position will affect means-tested public benefit programs. Examples of these programs include supplemental security income, Medicaid, AIDS Drug Assistance Programs (ADAP), and Supplemental Nutrition Assistance Programs. Eligibility for these benefits and/or the amount of benefit that one receives is determined in part by income. Because the federal government has now indicated that it will apply income-splitting for federal tax purposes, it is reasonable to anticipate that it may apply income-splitting to calculate the amount of a person's income for other federal purposes as well, such as means-tested public benefits, especially those requiring submission of one's income tax return(s) with one's application. For example, AIDS Drug Assistance Programs are a set of state-administered programs that provide HIV medication to low-income individuals. Financial eligibility for these programs varies from state to state, but someone who is currently eligible for ADAP and whose recognized income will increase due to income-splitting may become ineligible as a result. Conversely, a person whose income was too high to be eligible for ADAP but whose recognized income will decrease as a result of income-splitting may subsequently qualify for ADAP.

20. Where can I find more information about the new IRS position?

More information about the new IRS position is available from a number of sources, including the following:

- The new IRS position was released as Chief Counsel Advice 201021050 (available at www.irs.gov/pub/irs-wd/1021050.pdf).
- The new IRS position was further explained in Private Letter Ruling 201021048 (available at www.irs.gov/pub/irs-wd/1021048.pdf).
- As a result of the new IRS position, the IRS is now advising California RDPs to consult IRS Publication 555 (available at www.irs.gov/pub/irs-pdf/p555.pdf) and to follow the advice given there for married taxpayers filing separately regarding how state community property law treatment affects federal taxes.

  Note: *When consulting IRS Publication 555, it is important to note that some of the advice in the publication is based on the federal filing status of "married filing separately" (a filing status that, like "married filing jointly," is currently unavailable to California RDPs), not community property law.*
- California RDPs are also encouraged to refer to FTB Publication 737 (available at www.ftb.ca.gov/forms/2011/11_737.pdf) for guidance on how RDPs are treated for *California* income tax purposes.
- Same-sex married couples in California are also encouraged to refer to FTB Publication 776 (available at www.ftb.ca.gov/forms/2011/11_776.pdf) for guidance on how same-sex married couples are treated for *California* income tax purposes.

[19] Nevada law does not treat RDPs registered in other states as Nevada RDPs, unless the couple also registers with Nevada. See NRS § 122A.500.

[20] If you are a Nevada RDP who applies community property treatment to your federal tax return and the IRS questions your doing so, you can contact Lambda Legal's Help Desk at (213) 382-7600 ext. 330 to let us know.

In addition to reviewing those publications and other sources of information, same-sex couples should consider consulting a tax professional with expertise in this area about how the new IRS position may affect their particular situation. Neither these Q&As nor the above materials can substitute for individualized advice about how this new IRS position may affect you.

Lambda Legal is the oldest and largest nonprofit legal organization advocating nationally for full recognition of the civil rights of lesbian, gay, bisexual and transgender ("LGBT") people and those living with HIV through groundbreaking litigation, education and public policy work. Since 1973, Lambda Legal has appeared as counsel or friend-of-the-court in hundreds of cases in state and federal courts on behalf of LGBT people who have suffered discrimination because of their sexual orientation or gender identity, including a great many cases seeking to protect and find remedies for same-sex couples and their children who have suffered severe, needless harms because their family relationships are not respected as heterosexual couples' relationships are. Lambda Legal attorneys drafted AB 205, California's broad domestic partnership rights and responsibilities law enacted in 2003, and subsequent legislation that expanded and clarified the rights and responsibilities of registered domestic partners in that state, including the 2006 legislation that secured state income tax equality. Lambda Legal attorneys currently provide consultation nationally to local, state and federal policymakers concerning the legal needs of same-sex couples and their families, and the serious harms inflicted by our country's continuing, unjust discrimination against them.

Lambda Legal gratefully acknowledges the generous assistance of Irell & Manella LLP in preparing this document, and also thanks Wendy E. Hartmann of the Bennett & Erdman law firm for her thoughtful suggestions and ongoing assistance with tax and estate planning matters generally.

For more information, please contact the Help Desk in Lambda Legal's Western Regional Office, 3325 Wilshire Boulevard, Suite 1300, Los Angeles, California 90010.
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Se habla Español tambien.

NOTICE: These Q&As provide only general information, and simplify complex legal and tax matters for the purposes of presenting that general information. As a result, they may not summarize the relevant law in ways that could be relevant to you, and may omit issues that could be significant in your situation. In addition, tax laws and official interpretations of them are constantly changing and are subject to differing interpretations. Further, these Q&As are provided with the understanding that, by doing so, Lambda Legal is not rendering tax, legal, accounting or other professional advice to you. Lambda Legal assumes no liability whatsoever in connection with any use of these Q&As. Accordingly, no one should rely on these Q&As when making decisions or taking actions with respect to any tax, legal or accounting matter. Lambda Legal urges you to consult your own tax, legal and/or accounting advisers about your individual situation before making any decisions or taking any actions. In accord with Internal Revenue Service Circular 230, only formal opinions satisfying specific requirements may be relied on for the purpose of avoiding certain penalties under the Internal Revenue Code. These Q&As do not constitute a formal opinion satisfying such requirements. Accordingly, Lambda Legal advises you that nothing in these Q&As is intended to be used, and nothing herein can be used, by you or any other person as such an opinion for the purpose of avoiding penalties imposed under the Internal Revenue Code.

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Lambda Legal's work on this document is generously funded by the Anita May Rosenstein Foundation. Anita May Rosenstein has created The Dana Schwartz Educational Fund to raise the money that Lambda Legal needs to litigate, educate and reform public policy in California, so all same-sex couples receive the respect and protections they deserve.