

## Community Property FAQs

In 2010 there were major changes in the federal tax preparation guidelines for Registered Domestic Partners and Same-Sex Married Couples living in community property states with recognition. The IRS specifically addressed California, Nevada and Washington. Arguably same-sex couples living in New Mexico should be filing under the same guidelines. [Click here](#) to read the opinion from New Mexico's Attorney General on same-sex marriages performed outside of the state.

Please note that this is an emerging topic and there is some disagreement regarding the IRS answers. The IRS guidance is not "authoritative" on this subject. Particularly if you are self-employed, it is recommend that you seek guidance from a competent tax professional to discuss the issues regarding the treatment of self-employment income under a community property scenario.

Also note that the determination of community property or separate property is a legal determination and it could have legal consequences not only for federal income tax purposes but also for federal gift tax purposes, for disposition of assets on the dissolution of relationships and for disposition and taxation of assets upon death. Please undertake this determination very seriously – you may need the help of an attorney to do so. None of the information here can be construed as valid legal advice: this is information of a general nature and should be taken as such. Due to the complexity, it is recommended that you to seek legal counsel from an attorney specializing in this area.

## FAQs

**Does the [2010 CCA ruling](#) mean we can now file our federal returns as Married Filing Jointly or as Married Filing Separately?**

No. The ruling does not recognize your relationship, per se, and the IRS has indicated that as such you cannot file your returns as married. Your filing status remains either "single" or "head of household" (if you qualify to file as head of household). What the ruling does say is that for federal tax purposes your community property rights will now be recognized.

**What about President Obama's announcement about the Defense of Marriage Act (DOMA) being unconstitutional, and the other courts all declaring DOMA unconstitutional – doesn't that mean I can file my federal tax return as Married Filing Jointly?**

No, *probably not*. While President Obama's announcement is a wonderful step toward equality the announcement instructs governmental agencies, including the IRS, to still enforce DOMA until the Supreme Court rules on the issue, even though the Department of Justice believes DOMA to be unconstitutional. Therefore, the

announcement does not directly alter how you can file your federal income tax return. You still *probably* cannot legally file a "married" federal income tax return as an original return without specific legal disclosures. However there have been a number of court cases that declare DOMA unconstitutional and if you would like to file a "married" federal income tax return based on those court cases, you should discuss this possibility with your tax preparer and perhaps an attorney specializing in this area who can explain the benefits and risks to you. You might also want to consider filing a **protective claim** if you would save federal income tax by filing a "married" federal income tax return. This is a time limit on protective claims and you should discuss this option with your preparer immediately to gain the maximum benefit. This is especially important for couples living in non community property states who cannot avail themselves of income splitting as explained below.

**So what exactly does it mean that the federal government is recognizing my community property rights? What are community property rights?**

Some states are "community property states." When you enter into a legal intimate relationship – "a community" in these states – the state may grant you community property rights. This means that all earnings from your own efforts (i.e. your W-2 wages or your self-employment income) while you are "in community" (i.e. after the date you became registered domestic partners or got married) automatically belongs equally to each partner of the community. So if one spouse works and earns \$100,000 and her wife does not work, they each own \$50,000 of the first spouse's \$100,000 W-2 income. In the past the IRS ignored this fact and told the spouse to report her \$100,000 of W-2 income on her own federal tax return. Now, they recognize community property rights and each spouse reports \$50,000 on their individual federal tax return.

**What does this mean in terms of how much federal income tax I owe?**

Many couples, particularly those in which there is a big difference between their incomes, will pay less federal income tax overall. In my example where one spouse works and makes \$100,000 and the other spouse doesn't work at all, this couple could save more than \$6,000 per year by being able to split the \$100,000 of income between the two tax returns. Some couples save even more, ranging from savings of \$20,000 per year in federal income taxes to one couple who saved more than \$34,000 for a single year. But not every couple will save, and some may even pay more federal tax. While it appears there are many more couples who will pay less tax than there are couples who will owe more tax, the effect on your own personal taxes will depend on the totality of your tax situation. Many factors matter such as:

- Whether you have children and who deducts them.
- If one or both of you claimed head of household status in the past.
- Whether you have a mortgage and who pays it.
- Who claims the interest deduction and how high the state income tax rate is in the state where you live.

- If either of you have significant separate property income, whether either of you qualify for tax credits.
- If either of you are in Alternative Minimum Tax now, or if you will go into Alternative Minimum Tax once your community property and deductions are split.

It is nearly impossible to determine whether you will save tax, but if your incomes are wildly different it is probably more likely that you will, although even then, not guaranteed.

**What about other income? We also have interest income and some dividend income.** Whether your interest income and your dividend income is "community property" or not depends on which state you live in. Some community property states like Louisiana say that any income you receive from any source while you are married is community property. But other states, like California, say it depends on whether you are earning interest on funds that were originally community property or not.

**Huh? Funds that were originally community property? Can you explain?**

Yes, if in my prior example the couple took \$10,000 out of the \$100,000 W-2 income and put it in a savings account and it earned \$100 in interest, that \$100 of interest is community property too, because the money that earned it, the \$10,000, was community property. But if before they ever got married one had a savings account that had \$10,000 in it and that was the only money in that account, and that account earned \$100 of interest, then that \$100 is not community property because the funds that earned it were not community property, they were separate property.

**Ok, so now I understand when the interest is community property and when it is separate property, but how does that affect my federal income tax return?**

Like your wages you also need to divide the rest of your income into community property and separate property. If the \$100 of interest is community property then you will each report \$50 on your federal tax returns. If the \$100 is your separate property then you report all of it on your own tax return. So in the examples above, so far I have \$50,000 of W-2 income to report, \$50 of community property interest income to report and \$100 of separate property interest income to report on my tax return.

**But what if our community property savings account is only in my name and the 1099-Interest form that the bank sends to us only has my social security number on it? Can I just put it all on my tax return then?**

No, the name on the account does not determine whether or not the account and the income are community property or separate property and it makes no difference whose social security number is on the form. What matters is the source of these funds and whether the interest is from community property funds or separate property funds. Let me repeat because this is often confusing for people, **it generally does not matter**

**whose name is on the account, nor does it matter whose social security number the interest is reported to.** What matters is whether the funds that are in the account – or used to pay the expense – are community funds, separate property funds or a combination of both that may need to be split into their community property and separate property elements.

**So I heard that I can efile my tax return for 2012, is that true?**

While technically the IRS is able to accept an efiled tax return, most tax software cannot calculate the correct tax and efile the return. The software companies are trying desperately to provide software for efilings and the IRS has a new [form 8958](#) to help with efilings. Although far from perfect at this time, some people may be able to efile. The IRS requires that you attach a summary to your federal tax return that shows how you divided up the items of income and deduction that are community. You can access a copy of [Publication 555](#), which you should read before you meet with your tax advisor or before you complete your own tax returns.

But please take caution when reading Publication 555. Although it was updated by the IRS for the new rules in December 2010, parts of the publication can be confusing and parts of the publication are most likely incorrect and should be changed. Interested parties are currently in communication with the IRS in this regard but it is unclear how the IRS will respond.

Also, various portions of Publication 555 only apply to partners who are no longer living together and other sections only apply to taxpayers who file as “Married Filing Separately.” Under current DOMA restrictions, you cannot file your tax return as “Married Filing Separately” and these rules should not apply to you. Be certain you read this publication carefully. In certain circumstances even when you follow the instructions in the publication, you are likely to get correspondence from the IRS after you file your tax returns. The IRS correspondence has lessened since 2010 filings.

**Can I still have my tax refund directly deposited if I paper file?**

Yes, you can still request that your refund amount be directly deposited to your bank account, but you should be aware that it has typically been taking about four weeks for the paper filed tax returns to be processed by the IRS and for refunds to be issued. Efilings when possible this year may result in quicker refunds.

**Will the commercial tax software programs be able to complete my tax returns this year?**

Maybe. Just in the last few weeks have commercial programs become available and early reports indicate that there may still be bugs in the software, but the providers are being responsive and working these out. If there are any complicated calculations or if you and/or your tax preparer agree to report differently from the current IRS

guidelines (especially around self employment income) the software may need to be overridden or it may be easier to paper file at this time.

**So does the tax software used by the tax professionals complete these returns?**

Until providers get the bugs worked out, the tax software that professional tax preparers use, in and of itself, does little to help complete the tax returns, but the tax professionals should be able to manipulate the tax software program and produce an accurate tax return for you if they are savvy regarding these changes and the nuances of the new rules. It is extremely important that you have a tax preparer who is conversant with these issues.

**That sounds complicated, and expensive?**

Correct. For the next few years these tax returns will be complicated and expensive to complete, even for the tax professionals. These next few years will be challenging for you and the tax professionals who complete these returns. It is likely to be expensive if you hire a professional. And you or your preparer may need to file an extension in order to get your tax returns completed correctly.

**I've never filed an extension before; doesn't the IRS frown on extensions?**

Not at all, extensions are a normal part of business with the IRS. You still pay your taxes on time because the extension doesn't give you more time to pay your taxes if you owe tax, it just gives you more time to get the tax forms done correctly. This makes it easier for both you and the IRS because then you do not have to amend your returns later if you filed them incorrectly in the first place.

**But what if I already filed my tax returns and got my refunds even, but now I realize that I didn't do it correctly?**

Don't panic if you've already filed your tax returns and did them incorrectly, the IRS will not show up at your door tomorrow. In fact, it will take a while before they will even be able to match up your tax returns to know whether you live in a state that grants you community property rights. If you've already filed your return and it's wrong, my best advice is to consult with a tax professional who can file an amended tax return for you (most likely after April 15th).

**I heard something about needing to change my tax returns for prior years. Can you explain?**

Amending prior year returns is **not required**, but it is permitted for returns that are still open assuming you were married (and/or registered living in a community property state) in those years. If you would pay less federal income tax under the community property splitting rules then you have the option of amending prior year returns. Of course if you owe more tax you would not amend your returns. How much you save, or if you save, all depends on your particular tax situation. And completing these amended returns may be expensive as well.

Note: Most 2009 tax returns and later are still open for amendment.

**Is there a deadline for filing amended returns?**

Yes, there is a deadline that is dependent on when you actually filed your original returns. But for many people the 2009 tax returns must be amended by April 15, 2013.

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