



Kimberlee Sipe Financial Advisor

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How Financial Planning Has Changed for Same-Sex Couples

Retirement & estate planning strategies are being greatly altered.

Provided by Kimberlee D. Sipe

When the Supreme Court affirmed the legality of same-sex marriage in June, its ruling profoundly altered the financial planning landscape for gay and lesbian couples – resulting in some “night and day” differences.

Yet in looking at the financial “before and after,” same-sex spouses and their advisors must also consider the “when and where” – because the Supreme Court ruling only applies to the 13 states that allow same-sex marriage (and the District of Columbia). Gay and lesbian spouses are still waiting to see if financial benefits will be granted in all 50 states.^{1,2,3}

Here is how the landscape has changed for married gay and lesbian couples in states recognizing same-sex marriage.

Income taxes. When DOMA was in effect, same-sex spouses couldn't file joint federal tax returns. Now they can. Filing jointly does not always result in a tax savings; for an extremely high-earning married couple, it can be a bad idea. Right now, single tax filers can earn up to \$400,000 before entering the 39.6% tax bracket; a married couple will enter it when their combined incomes surpass \$450,000. Still, same-sex couples are welcoming the option.⁴

Previous to the ruling, married same-sex couples faced a kind of “un-marriage penalty” in states without community property laws when one spouse far outearned another. In such cases, their federal tax bills were often higher than those of married straight couples. Qualifying for head-of-household status was difficult, as the higher-income spouse had to try to claim the other as a dependent. This was a no-go in community property states, in which the lesser-earning spouse's gross income stood little chance of falling below under the dependent exemption amount.⁵

The federal government often doubles or significantly raises the AGI threshold on tax law benefits for joint filers – benefits such as the Child Tax Credit, the qualified student loan interest deduction, and the taxable income exclusion of the gain on the sale of a primary residence. In addition to these benefits, a spouse in a same-sex marriage now gains the ability to deduct medical expenses and qualified tuition expenses incurred by the other spouse.⁵

Now that the chance to file jointly is available, could married same-sex couples get a federal tax refund by filing amended 1040s for the past three years of returns? It may be worth consulting an accountant to find out.

Social Security. Low-income spouses in same-sex marriages (think stay-at-home moms and dads) now have the chance to claim Social Security spousal benefits. If the other spouse passes away, being able to receive his or her larger Social Security payments could make a significant income difference. Another implication from the Supreme Court ruling: surviving spouses in a same-sex marriage could also be able to collect a deceased spouse's federal or military pension.^{1,4}



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Estate & gift taxes. Before the repeal of DOMA, life insurance was a core estate planning tool for wealthier same-sex couples. Sometimes an irrevocable life insurance trust containing a “Crummey provision” was created. Now, married gay and lesbian couples may want to reevaluate such insurance coverage because surviving spouses in same-sex marriages won’t have to pay federal estate tax on any inherited assets.^{2,5}

A spouse in a same-sex marriage can now make unlimited tax-free gifts to the other that will not count against the \$5.25 million lifetime gift tax exclusion, as long as the spouse receiving the gifts is a U.S. citizen. Same-sex married couples are now able to gift \$28,000 worth of property tax-free, per year, per recipient, just as straight marrieds can; previously, spouses in same-sex marriages were looking at the individual limit of \$14,000. (This is not to be confused with estate taxes some individual states require from their residents.)⁶

IRAs & 401(k)s. A surviving spouse in a same-sex marriage can now roll inherited IRA assets into their own IRA (provided they are named sole beneficiary of those assets). This opens the door for stretch IRA strategies among same-sex married couples. With federal recognition of gay and lesbian marriages, a surviving gay or lesbian spouse will have the ability to automatically inherit a 401(k) account unless that default beneficiary choice has been declined in writing by the account holder.^{1,2,4,7,8}

Workplace health benefits. Gay and lesbian couples are in line to save some tax dollars in 13 states and possibly others. Couples had to pay taxes on these benefits when DOMA was in place, even in states that recognized the legality of their marriages. Same-sex couples may wish to “shop around” and determine which employer offers a better or cheaper health plan.⁴

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What Marriage Equality Means Financially

The Supreme Court decision has brought significant change.

When the Supreme Court voted to repeal Section 3 of the Defense of Marriage Act (DOMA) on June 26, it opened financial doors previously closed to same-sex couples. Unfortunately, not all of these doors may open in certain states. A major complication must be resolved: while the high court’s opinion stated a legal principle, it didn’t say exactly how it should be applied.¹

Will the SCOTUS ruling apply in all 50 states? Gay and lesbian couples can now access marriage-based federal benefits in the 12 states permitting same-sex marriage (plus the District of Columbia). That is clear. Can these couples receive these benefits in the 38 states barring same-sex marriage? That is unclear. The SCOTUS ruling did not instruct these states to recognize the legality of gay and lesbian marriages performed elsewhere.^{1,2,3}

To complicate matters further, not all federal agencies define a lawful marriage using the same criteria. They look to state laws. Some determine the legality of a marriage by the “place of celebration” – that is, the state in which the marriage occurred. Others go by the state of current residence, in which a same-sex marriage may not be legal.¹

So will the Obama administration tell the IRS, the Social Security Administration and the Department of Veterans Affairs to use the “place of celebration” marriage standard with regard to all federal benefits? It remains to be seen. Here is what is changing as a result of the ruling in 12 states and possibly others.

Same-sex couples in 12 states can now file joint federal tax returns. Both married couples and partners may now file jointly. This move may not always produce a tax savings, but it sure is nice to have the option.²

In these 12 states, same-sex couples may now access federal benefits. In terms of Social Security, a surviving spouse in a same-sex marriage now has the option to switch to a deceased spouse’s benefits if they are greater. Gay and lesbian spouses may now plan Social Security

strategies that can potentially increase retirement income, such as one spouse claiming Social Security early and later switching to spousal benefits. Same-sex couples living in states that recognize gay marriage are now eligible for federal government employee spousal pension benefits as well, and have equal access to the Family and Medical Leave Act. The federal Office of Personnel Management said on June 28 that it would give equal health and pension benefits to “all legally married same-sex spouses” regardless of where they live.^{1,2,4}

Assets may pass to a surviving spouse without risk of estate tax. The SCOTUS ruling paves the way for one spouse in a same-sex marriage to leave an unlimited amount of assets to a surviving spouse. Prior to the ruling, a surviving spouse faced the possibility of paying federal estate taxes on inherited assets from a spouse if they exceeded \$5.25 million. High net worth gay and lesbian couples commonly bought life insurance to address the possibility of this estate tax burden. Now, they may need less insurance coverage.⁴

No taxation of employer-sponsored health benefits. Thanks to DOMA, same-sex spouses had to pay taxes on these benefits – a cost averaging c. \$1,000 year. The June 26 Supreme Court decision announced an end to all that. It also mandated that employees married to same-sex spouses receive COBRA coverage.^{4,5}

Businesses face question marks. Employers have been given a mission – the benefit plans they sponsor now must comply with the change in federal law. The largest employers have the toughest assignment here, as what is now legal in one state may not be in another. They are anxiously awaiting guidance from the IRS, the DOL and the White House, but who knows how quickly it will arrive. It should be noted that roughly 62% of Fortune 500 firms offer same-sex domestic partner health benefits; that percentage may soon increase.⁵

Beyond health benefits, the SCOTUS decision also affects retirement plans like 401(k)s, 403(b)s, pensions, and IRAs. Under federal law, heterosexual spouses inherited such retirement accounts by default unless the beneficiary form signed by the deceased spouse dictated otherwise. Now surviving gay and lesbian spouses will be able to count on the same thing.^{4,6}

Are gay & lesbian couples eligible for retroactive tax treatment? Here is another unresolved question. It is possible that married same-sex couples can pursue tax breaks in tax years that are still open (2010-12)?²

Now is a good time for same-sex couples to revisit their financial and estate plans, with the hope that the federal government acts quickly to resolve the legal ambiguities.

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