

## BREAKING DOWN THE “DOMA” DECISION

In 2004, Massachusetts became the first state in the United States, and the sixth jurisdiction in the world, to allow same-sex marriages. The Massachusetts Supreme Judicial Court determined in *Goodridge v. Department of Public Health*, that it was unconstitutional under the Massachusetts Constitution to deny same-sex couples the right to marry, but to permit marriage for heterosexual couples.

Despite the legalization of same-sex marriages in Massachusetts, the “Defense of Marriage Act” (“DOMA”) enacted in 1996 by the U.S. Congress was still in effect. Under Section 2 of DOMA, a State is not required to give effect to any public act or judicial proceeding of any other State which respects the relationship between persons of the same sex that is treated as a marriage under the laws of such other state. Section 3 of DOMA required same-sex spouses to be treated as unmarried for purposes of federal law. Massachusetts’ ruling in *Goodridge* created a discrepancy between State and Federal protection. Some states offered same-sex married couples state sponsored benefits, while the Federal government denied federal benefits to those same couples.

In June 2013, the United States Supreme Court struck down Section 3 of DOMA in *United States v. Windsor*, stating that Section 3 was unconstitutional because it violated liberty and equal protection rights guaranteed under the Fifth Amendment.

The Court’s ruling leaves Section 2 intact which gives States the authority to define marriage. The decision does not guarantee all same-sex couples the right to marry, but it allows people who marry in states permitting same-sex marriage to receive the same federal benefits offered to heterosexual couples.

### How did the DOMA case arise?

Thea Spyer and Edith Windsor, a same-sex couple (legally married in Ontario, Canada), were residing in New York, a state that legalized same-sex marriage. Spyer passed away in 2009 and left all her property to Windsor. The IRS denied Windsor’s attempt to claim the federal estate tax marital deduction for transfers to surviving spouses, and compelled Windsor to pay \$363,000 in federal estate taxes. Windsor sought a refund and filed suit in 2010, claiming that DOMA unconstitutionally singled out legally married same-sex couples without justification.

### What was the Supreme Court’s decision?

Supreme Court Justice Anthony Kennedy wrote the 5-4 decision stating that DOMA’s definition of marriage violated the Fifth Amendment and could not be used to deny legally married same-sex couples the same federal benefits available to heterosexual married couples. The decision did not address the remainder of the DOMA statute, and therefore each State retains the power to determine whether it will recognize same-sex marriages within its borders.

### What are the implications of this decision?

The tax consequences of this change are significant, since almost 200 provisions of the Internal Revenue Code treat marital status as a factor for receiving a benefit or being subject to a limitation. In addition, there are over 1,000 federal protections and responsibilities attached to marriage. Under DOMA, same-sex couples were denied an extensive number of important protections and responsibilities.

- **Income Tax Implications**

The U.S. Department of the Treasury and the Internal Revenue Service (“IRS”) recently ruled, in light of the repeal of DOMA, that same-sex couples legally married in a jurisdiction which recognizes same-sex marriage will be treated as married for all federal tax purposes, even if the same-sex couple now lives in a jurisdiction that does not recognize same-sex marriage. This change is effective as of September 16, 2013. However, this ruling does not apply to registered domestic partnerships, civil unions or other formal relationships that may be recognized under state law.

After the Supreme Court’s decision in *United States v. Windsor* and the IRS ruling, all married couples are able to take advantage of combining income, deductions, tax credits and brackets. This is likely to reduce the tax liability of a spouse with a high income if the other spouse has a lower income or does not work. This may also cause a “marriage penalty” if the incomes of each spouse are similar and substantial. The IRS allows a person to file an amended tax return for a refund on the later of (1) three years from the date the return was filed or (2) two years after the date the tax was paid. This means that couples who have been married since 2010 may re-file their tax returns for the years that they have been married in order to receive the previously denied tax benefits. It is important for couples to review their finances and determine whether filing amended returns is beneficial. It is essential to note however, that although same-sex spouses may now file jointly for federal purposes, they will still need to file as single for state purposes in states which do not allow same-sex marriage.

- **Estate and Gift Tax Implications**

One of the most important implications of the Supreme Court’s decision is the effect on federal estate and gift taxes. There are a number of favorable estate and gift tax provisions for married couples which are now available to same-sex married couples. Under federal law, any U.S. citizen is allowed to pass an unlimited amount of property to his or her U.S. citizen spouse tax-free during life and upon death. Under DOMA, since a same-sex spouse was not considered a legal spouse, any transfers made between same-sex spouses were subject to estate and gift tax, and treated as a gift or bequest to an unrelated party. Prior to the Supreme Court’s decision, even same-sex married couples living in states that recognized same-sex marriage were disproportionately burdened by estate and gift taxes. Now, same-sex married couples may utilize the unlimited marital deduction to transfer an unlimited amount of property to one another, free of federal gift and estate tax.

Additionally, after DOMA, same-sex married couples will be able to enjoy the benefits of portability and take full advantage of the Federal Applicable Exclusion Amount, currently set at \$5.25 million. This exclusion allows a person to pass up to \$5.25 million dollars during their life or at death to any individual

without incurring an estate or gift tax liability. If a spouse does not use their entire allotted exclusion amount, the surviving spouse may use the remainder of the deceased spouse's applicable exclusion amount, referred to as portability, and pass property to descendants or other beneficiaries. The surviving spouse may combine the deceased spouse's unused applicable exclusion amount with his or her own applicable exclusion amount (currently up to \$10.5 million) to make additional tax free gifts or reduce estate tax liability.

- **Gift Splitting**

Same-sex married couples may now "gift split", meaning that gifts to individuals are treated as if made one-half by each spouse. The current annual gift tax exclusion amount is \$14,000 per donee. Together the couple may then gift up to \$28,000 per year to any individual without using any portion of their \$5.25 million exclusion amount or incurring gift tax liability that year.

- **Retirement Accounts**

Same-sex spouses now have the rights of heterosexual spouses with respect to retirement plans. A married same-sex spouse may now contribute to his or her spouse's retirement plan account. If the surviving spouse is a beneficiary of the deceased spouse's retirement plan, then the surviving spouse may rollover the retirement funds into his or her own retirement account. Additionally, the surviving spouse may delay taking Required Minimum Distributions until April 15<sup>th</sup> of the year following his or her attaining the age of 70½.

- **Life Insurance Policies**

Same-sex spouses now have the same rights as heterosexual spouses with regard to life insurance. In the past, same-sex couples often named their spouses as the beneficiary of a life insurance policy or used a life insurance trust to pass life insurance proceeds to the surviving same-sex spouse. With recognition of same-sex marriages and the use of the unlimited marital deduction, same-sex couples may purchase joint and survivor life insurance policies which would allow them to provide tax free life insurance proceeds to their children or to other beneficiaries upon the death of the surviving spouse.

- **Social Security**

Same-sex married couples are now eligible to apply for social security benefits on a spouse's earnings and for survivor benefits after a spouse's passing.

- **Health Insurance, Hospital Visitation and Medical Leave**

Same-sex married couples may now enjoy increased benefits with respect to health insurance, be granted hospital visitation, and even medical leave to care for a sick or injured spouse. A same-sex married employee who is covered under an employer's health insurance plan may exclude the premium amount paid by the employer to cover the employee's same-sex spouse from his or her gross income. Prior to the Supreme Court's decision, if a plan covered the non-employee spouse, the employee spouse was taxed on the estimated value of the coverage. Further, an employee spouse may now pay the

premiums for the same-sex spouse with pre-tax dollars under an employer-sponsored cafeteria plan. When deciding whether to amend tax returns for open tax years, married couples may wish to consider the tax implications of health insurance premiums.

### **What Wilchins Cosentino & Friend LLP Can Do For You**

The experience of the Private Client Services Group at Wilchins Cosentino & Friend LLP combines more than 75 years of providing high net worth individuals with legal and tax planning advice for their estates, trusts, business activities, investments and insurance. Our multi-disciplined team of attorneys can provide personalized advice regarding your estate planning needs and explain how the repeal of DOMA and the IRS ruling may impact your estate plan, tax rights and obligations.

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