

In U.S., same-sex spouses may face financial tangles

By Temma Ehrenfeld
8 MIN READ

NEW YORK (Reuters) - Christel de Vries, a Dutch outsourcing manager for Accenture, sealed her love for her female partner twice, once in 2001 in Amsterdam under Dutch law and again in 2007 in a civil union in New Jersey. Yet under U.S. federal law, she isn't married — and that is creating obstacles in her divorce.

The 1996 Defense of Marriage Act rejected federal recognition of same-sex marriages in the United States and abroad and declared that no state need recognize a same-sex marriage in another state. The conflict between state and federal law — and between states — creates double worlds for gay marrieds in nearly every area of their financial lives.

Last week, the U.S. Appeals Court in Boston ruled that DOMA unfairly denies federal benefits to same-sex couples married under state law. The decision would apply to couples in the First Circuit, where Massachusetts, Vermont, New Hampshire and Connecticut allow people of the same sex to marry.

However, the court put a stay on its decision until the next step in the appeals process, most likely a Supreme Court ruling.

“If this decision is upheld on appeal, it should pave the way for a wide swath of federal protections for married same-sex couples,” said Susan Sommer, director of constitutional litigation for Lambda Legal in New York.

But in the meantime, and despite the broadening support from President Barack Obama and others for the rights of gay people to marry, they still face more paperwork and legal issues - and costs - than heterosexual couples.

“A lot of gay couples are getting married because they can, not because they’ve thought through the legal consequences,” said Larry Jacobs, a Rockville, Maryland, estate and trust attorney specializing in same-sex couples. Jacobs often discusses pre- and post-nuptial agreements with clients to sidestep these knots.

DIVORCE COSTS MORE

When de Vries and her partner separated in 2009, a New Jersey judge ordered de Vries to pay spousal support. But unlike a federally-recognized spouse, she cannot deduct those payments from her federal taxes — costing her an extra \$12,000 a year, she estimates.

ADVERTISEMENT

When their civil union is finally dissolved, a New Jersey judge will issue a qualified domestic relations order that will require de Vries to give her partner a chunk of her 401(k). But federal law governs these retirement plans, and de Vries says her company cannot distribute the money unless she leaves the firm. And her former partner cannot roll any such payment into a retirement account, so it, too, would be subject to taxes.

“I guess we’ll have to assume that the discriminatory law will change,” de Vries said.

FILING FOUR TAX RETURNS

Gay marrieds usually prepare four tax returns. In most states, they file a joint state tax return. Because the joint state return requires certain federal numbers, “you prepare a federal joint return, pull the numbers off it and throw it away,” said Jacobs.

Then they prepare two federal returns as singles. That’s often a good deal: A higher earner can take more of deductions like mortgage interest and real estate or claim a child and file as “head of household,” said Dana Levit, a financial planner at Paragon Financial Advisors in Newton, Massachusetts.

However, since 2010, an Internal Revenue Service ruling has required that in states with both “community property” laws and same-sex unions, gay couples must split their earnings evenly on their individual tax returns.

Los Angeles financial planner Carol Grosvenor and her spouse Marilyn, an Episcopal priest, saw a bump in taxes of \$6,000 a year because of this rule, according to Grosvenor.

Confusion reigns. “It’s hard to find a tax preparer in California that even understands the rules,” Grosvenor said.

Karen Mateer, a Pasadena-based tax, trust and estate attorney, advised a gay couple who moved from California to Arizona at mid-year. “Their taxes were a mess because the rules were completely different in the two states,” she said. In California, they were married; in Arizona they weren’t.

ADVERTISEMENT

ESTATES TAKE MORE PLANNING

Thom Johnston and Bob Gould moved from San Francisco to Fort Wayne, Indiana, nine years ago, to help Johnston’s mother and to cut their expenses. Selling their San Francisco home allowed them to buy a house in Fort Wayne mortgage-free.

But at the time, Indiana’s estate tax law came down hard on “unrelated” heirs, and Indiana did not recognize the couple’s California civil union. So they’ve bought two pricey life insurance policies to cover those taxes if either man dies. “We watch our expenditures carefully for several months before we make the annual payments. They are painful checks to write, knowing that we wouldn’t be doing it if our marriage was recognized in Indiana,” said Johnston.

That Indiana provision is now being phased out, but federal estate law still penalizes same-sex spouses who inherit property from their

partners. Under federal law, a spouse can inherit an estate of any size without owing estate taxes. A same-sex partner must pay estate tax on an inheritance above \$5 million, and unless Congress acts, that amount will drop to \$1 million on January 1, 2013.

For Mateer's gay clients, she said, "It may mean selling a home or business to raise cash to pay death taxes."

Men and women who are married can give each other money without considering taxes. Between gay spouses, gifts above the current \$13,000 annual limit generally incur either a gift tax or reduce the lifetime exemptions before estate taxes apply.

MOST VULNERABLE WIDOWS AND WIDOWERS

Gays without income and savings of their own are especially vulnerable when a partner dies. They are ineligible for the Social Security "widow benefit," which lets surviving spouses take the deceased's full Social Security payment.

And while state laws typically protect spouses from being cut out of a will, many of Jacobs' gay clients live in houses they won't inherit, he said. In one case, a client was kicked out of the house two weeks after her partner died - by the partner's family. A Maryland probate judge ruled that she had no claim.