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SAME-SEX MARRIAGES – THE QUAGMIRE CONTINUES AFTER *WINDSOR*[1]

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INTRODUCTION.

On June 26, 2013, the United States Supreme Court issued a historic decision affecting the application of federal law to same-sex married couples. This decision will have far reaching consequences, but the breadth, applicability and consequences of this decision are uncertain.

WINDSOR.

The case of *United States v. Windsor*[2] ("***Windsor***") held that Section 3 of the 1996 Defense of Marriage Act[3] ("**DOMA**") was unconstitutional as a deprivation of liberty protected by due process and equal protection. Section 3 of DOMA stated that for purposes of federal law, the word "marriage" meant only a legal union between one man and one woman as husband and wife, and the word "spouse" referred only to a person of the opposite sex who is a husband or a wife. In effect, DOMA denied federal benefits, rights and privileges to the partners/spouses of same-sex marriages.

> **DOMA**
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> **Section 2**. No state is required to treat any same-sex couple married under the laws of another state as married. [NOT ADDRESSED BY *WINDSOR* COURT.]
>
> **Section 3**. In interpreting any federal statute, regulation, ruling or guideline, the word "marriage" means only a legal union between one man and one woman as husband and wife, and the word "spouse" refers only to a person of the opposite sex who is a husband or wife. [DECLARED UNCONSTITUTIONAL BY *WINDSOR* COURT.]

In *Windsor*, a same-sex couple residing in New York went to Canada to marry and then returned to New York. While living in New York, one of the spouses to the marriage died and the issue was whether the decedent's estate would be entitled to the same federal estate tax benefits that would be accorded to opposite-sex marriages of persons living in New York. At the

[1] This article is adapted from an article that will appear in the Autumn 2013 issue of *Willamette Management Associates Insights.*

[2] 570 U.S. _____, 133 S. Ct. 2675 (2013).

[3] 1 USC §7; 28 USC §1738C.

time of the spouse's death, New York recognized same-sex marriages. The *Windsor* Court concluded that Section 3 of DOMA was unconstitutional and, therefore, the decedent's estate was entitled to the same federal estate tax benefits that a heterosexual couple would have received.

Therefore, it is clear from the *Windsor* opinion that a same-sex married couple residing in a state that recognizes same-sex marriages will be entitled to all federal benefits, rights and privileges accorded to opposite-sex married couples in that state.

The uncertainty at this time is whether federal benefits, rights and privileges will be accorded to same-sex couples validly married in one state but thereafter residing in another state at the time in question that does not recognize same-sex marriages, such as Texas, Florida, Pennsylvania and many others. *Windsor* is only the first step in unraveling the quagmire facing same-sex married couples.

The *Windsor* Court did not address Section 2 of DOMA, which states that one state does not have to recognize a marriage performed under the laws of another state.

PERRY.

On the same day as the issuance of the *Windsor* opinion, the United States Supreme Court also issued a decision in the case of *Hollingsworth v. Perry*[4] ("***Perry***"), in which the Court held that neither the Court nor the lower Federal Circuit Court had the authority to decide the question of whether California Proposition 8 was unconstitutional as held by the Federal District Court. California Proposition 8 stated that only a marriage between a man and woman is valid or recognized in California. The Federal District Court concluded that Proposition 8 was unconstitutional. As a result of the Supreme Court's decision, the Federal District Court's original opinion held and, therefore, Proposition 8 remained unconstitutional and same-sex marriages in California are permitted.

STATES RECOGNIZING SAME-SEX MARRIAGES AS VALID.

At the present time, thirteen (13) states and the District of Columbia recognize same-sex marriages (SSM) as valid. Those states are New York, California, Massachusetts, Connecticut, Iowa, Maine, Vermont, Maryland, Washington, New Hampshire, Minnesota, Rhode Island, and Delaware.

States that do not recognize same-sex marriages as valid will continue to contribute to the uncertainty facing same-sex married couples relative to federal law. For example, in 2011, the New Mexico Attorney General issued an advisory opinion that New Mexico can recognize same-sex marriages performed outside of New Mexico even though New Mexico itself does not recognize same-sex marriages. The effect of this advisory opinion is uncertain.

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[4] 570 U.S. _________, 133 S. Ct. 2652 (2013).

In Texas, a case presently is pending in the Texas Supreme Court wherein the issue is whether a Texas lower court had the power to grant a divorce to a same-sex couple who were married outside Texas and were living in Texas at the time of divorce.[5]

RECOGNIZED MARRIAGE REQUIRED.

The *Windsor* opinion does require a valid, recognized marriage. The status for federal purposes of civil unions and domestic partnerships after *Windsor* is uncertain. In the recent case of *Cozen O'Connor, P.C. v. Tobits,*[6] the federal District Court held "where a state recognizes a party as a "Surviving Spouse," the federal government must do the same with respect to ERISA benefits – at least pursuant to the express language of the ERISA – qualified Plan at issue here."[7] In this case, the same-sex couple was married in Canada and residing in Illinois, a state that does not issue marriage licenses to same-sex couples but does have a civil union statute.[8] The *Tobits* court treated the surviving party to an Illinois civil union as a "spouse" for purposes of the ERISA plan in issue.

However, the Internal Revenue Service ruled in 2010 that domestic partners in a registered domestic partnership in California who are treated as owning community property under California law would be required to report on the partner's individual federal tax return one-half of the community income.[9] These rulings did not treat the couple as married for federal purposes or extend any tax benefits to them as married. These rulings only addressed the nature of the property interest each partner had in the property and income.

For purposes of federal law, marriage is determined by state law. [10] As discussed below, the issue becomes which state law controls.

AFFECTED FEDERAL LAWS.

The General Accounting Office (GAO) issued a letter in 2004 that identified 1,138 federal statutory provisions involving marital status as of December 31, 2003, in thirteen (13) subject categories whose applicability depends on whether a couple is married. This letter is dated January 23, 2004, from Dayna K. Shah, Associate General Counsel, United Stated General Accounting Office to the Honorable Bill Frist, Majority Leader, United States Senate.[11]

Affected areas include, but are not limited to, income tax, gift tax, estate tax, immigration, social security, Medicare, Medicaid, family medical leave, veterans' spousal benefits, health insurance benefits for employee's spouse, spousal IRA rollovers, COBRA,

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[5] *State of Texas v. Angelique S. Naylor and Sabina Daly*, 330 S.W.3d 434 (Tex. App. Austin 2011, pet. filed).
[6] 2013 WL 3878688 (E.D. Pa., July 29, 2013).
[7] Id. at 4.
[8] Illinois Religious Freedom Protection and Civil Union Act, 750 ILCS 75/1.
[9] CCA 2010 21050; PLR 2010 21048.
[10] *See, Windsor,* 133 S. Ct. at 2689.
[11] The Letter can be found at www.gao.gov.

employee benefit plans, defined contribution plans, qualified domestic relations orders, HIPAA, cafeteria plans, flexible spending accounts, and health savings accounts.

The General Accounting Office issued a report in 2004 that identified 198 separate Internal Revenue Code provisions tied to marital status.[12]

WHICH STATE LAW CONTROLS.

The uncertainty arising out of the *Windsor* opinion is further exacerbated by the fact that all federal agencies currently do not apply the same standard for determining whether a same-sex marriage will be recognized for federal purposes. The issue revolves around the question of whether the state in which the marriage ceremony is performed ("**State of Ceremony**") or the state in which the married couple reside at the time in question ("**State of Residency**") will be used to determine whether the marriage will be recognized for federal purposes.

For example, Frequently Asked Question (FAQ) A-2 issued by Homeland Security, regarding an immigration visa petition, stated that "[I]n evaluating the petition, as a general matter, USCIS looks to the law of the place where the marriage took place when determining whether it is valid for immigration law purposes."[13]

In addition, after the issuance of the *Windsor* opinion on July 1, 2013, the Secretary of Homeland Security, Janet Napolitano, announced that effective immediately, the U.S. Citizenship and Immigration Services (USCIS) would immediately review immigration visa applications filed on behalf of a same-sex spouse in the same manner as applications filed for an opposite-sex spouse.

The Internal Revenue Service seemingly follows a State of Residency standard for determining marriage,[14] although in Rev. Ruling 58-66,[15] the Service concluded that a common-law marriage entered into in a state that recognizes such relationship would continue to be treated as a marriage for federal tax return filing purposes when that couple later moved to a state that requires marriage ceremonies. It is not clear how or if this Ruling applies to same-sex marriages today.

The Internal Revenue Service recently announced in "Answers to Frequently Asked Questions For Same-Sex Couples" that they are "….reviewing the important June 26 Supreme Court decision" on DOMA and "….will move swiftly to provide revised guidelines in the near future."

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[12] This report can be found at www.gao.gov/new.items/d04353r.pdf.
[13] www.dhs.gov/topic/implementation-supreme-court-ruling-defense-marriage-act; www.domaproject.org (foreign spouse of same-sex married couple living in Florida (a non-recognition state) granted green card by USCIS on June 28, 2013).
[14] *See,* IRS Publication 501.
[15] 1958-1 C.B. 60.

On June 28, 2013, the U.S. Office of Personnel Management issued a Memorandum stating that the Office of Personnel Management (OPM) will extend benefits to federal employees and annuitants who have legally married a spouse of the same sex. The benefits covered by this Memorandum are: health insurance; life insurance; dental and vision insurance; long-term care insurance; retirement benefits; and flexible spending accounts. The Memorandum implied that more benefits would be offered. The Memorandum did not mention which jurisdiction would be used to determine a legal marriage. Presumably, all that is required is the couple be legally married.

Until further federal legislation (such as the proposed Respect for Marriage Act pending in Congress[16]) or case law or guidance from each federal agency is issued, uncertainty will continue to exist for those same-sex married couples living in states that do not recognize same-sex marriages.

FEDERAL TAX LAWS.

The *Windsor* opinion has significant federal income, gift, and estate tax consequences for those same-sex married couples living in states that do recognize same-sex marriages ("**Recognition States**") and for those same-sex married couples living in states that do not recognize same-sex marriages ("**Non-Recognition States**").

It is important to note that *Windsor* and its application only relate to federal law, as states currently are entitled to treat same-sex couples differently. Thus, a situation could arise wherein a same-sex couple is recognized as married for federal tax purposes, thus requiring a married federal tax return, and not recognized as married under the laws of the state of residency, thus requiring an unmarried state tax return.

A. Income Tax.

1. Recognition States. Same-sex couples residing in Recognition States will now be required to file their federal tax returns as either married filing joint returns or married filing separate returns. Clearly, this filing status will apply for the tax return for the taxable year 2013 and subsequent years.

A question exists as to whether the *Windsor* opinion applies to a taxable year prior to 2013. For example, for a same-sex married couple in a Recognition State during the year 2012 but for which the 2012 federal tax return has not yet been filed, should that couple file the federal tax return for 2012 as married or as single.

One argument may be that since the *Windsor* opinion was not issued until 2013, the couple during the tax accounting year of 2012 were not considered as married for federal purposes. Therefore, this couple would have been considered as not married as of the close of 2012 and would have filed as separate single individuals. The contrary

[16] H.R. 2523; S.1236.

argument is the *Windsor* Court held Section 3 of DOMA to be unconstitutional, which has the effect of rendering Section 3 of DOMA void *ab initio* as though the statute never existed.[17] The latter argument would logically result in the conclusion that the same-sex married couple during the tax accounting period of 2012 were, for federal purposes, married and, therefore, should file as a married couple for federal income tax purposes.

The same analysis applies to years prior to 2012. A taxpayer generally does not have an obligation to file an amended return for a prior year.[18] Nevertheless, an issue arises whether an amended federal tax return[19] should be filed for a prior year with the status of a married couple if there is a benefit in doing so. Obviously, such a question would arise only if filing as a married couple for federal income purposes would result in an overall savings in income tax than the amount previously paid by each spouse to the same-sex marriage having previously filed separate single federal tax returns.

Furthermore, the issue arises as to how many prior years an amended return can be filed. The normal federal income tax statute of limitations on refund claims is three (3) years from the date the return was filed or two (2) years from the date the tax was paid, whichever is later.[20]

However, the last date to file a joint return for a prior year for which a single return was filed may be three (3) years from the due date (without extensions) of the prior year.[21] In that Ruling, however, the taxpayer could have filed a married, joint return for the prior year at the time the single return was filed. In the case of a same-sex married couple, that couple could not have filed a joint return for the prior year since federal law at that time precluded such a return. This distinction is important and makes this Ruling distinguishable from the situation confronting same-sex married couples seeking to file a married, joint return for a pre-*Windsor* year.[22]

If the normal statute of limitations on refund claims is applicable in this situation, then as of September 1, 2013, the earliest prior year for which a claim for refund could be filed would be either the tax year 2009 if the tax return was filed on October 15, 2010, or the tax year 2010 if the 2009 tax return was filed prior to September 1, 2010.

Until guidance is issued by the Internal Revenue Service, this uncertainty regarding claims for refund will continue to exist. However, prudence would dictate that

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[17] *See, Coral Springs Street Systems v. City of Sunrise*, 371 F.3d 1320 (11th Cir., 2004); *Summit Medical Associates v. James*, 984 F. Supp. 1404 (U.S. Dist. Ct., M.D. Ala., 1998), affirmed in part and reversed in part, 180 F.3d 1326 (11th Cir., 1999); Oliver P. Field, *Effect of Unconstitutional Statute*, Indiana Law Journal, January 1926.

[18] *See,* Treasury Regulations §1.451-1(a) and §1.461-1(a); *Broadhead v. Commission*, TCM 1955-3283. Treasury Department Circular No. 230 requires a practitioner to advise a client promptly of an error or omission and the consequences thereof but does not require the practitioner to advise the client to file an amended return.

[19] Form 1040X; claims for refund are made on an amended return.

[20] Section 6511(a) of Internal Revenue Code of 1986, as amended (the "**Code**").

[21] *See,* Rev. Ruling 83-183, 1983-2 C.B. 220.

[22] *See, Glaze v. United States*, 641 F.2d 339 (5th Cir. 1981).

claims for refund, even protective claims for refund, be filed as soon as possible for all years that would still be open under the applicable statute of limitations, provided there would be a net tax savings (refund) resulting from filing married as opposed to single.[23]

However, all transactions occurring during a prior year for which a claim for refund is being considered should be analyzed to determine if the federal tax treatment originally reported would change if the same-sex couple was now considered married in the year for which the amended return is filed. For example, if the spouses to a same-sex marriage each owned stock in a corporation and one spouse's stock was completely redeemed by the corporation during the prior year for which a claim for refund is being considered, the gain to the redeeming spouse in the original transaction might have been capital gain but now might be ordinary income because of the related party rules (the shareholders are now deemed married in the prior year).[24]

Another issue relates to same-sex married couples that are divorced. Clearly, for same-sex couples divorced in a Recognition State, such couples will be afforded the tax benefits of Code Section 1041 (tax-free property settlement), alimony under Code Section 71 (income to payee) and under Code Section 215 (deductible to payor) and child support under Code Section 71 (exclusion from income). However, for a couple that was granted a divorce prior to June 26, 2013, such couple should determine whether the property settlement and payments are entitled to a more favorable federal tax treatment than originally reported or if the divorce should be re-opened and restructured to take into account the tax benefits under the Code.

Another potential issue is whether a same-sex married couple in a Recognition State has a duty to treat an item for federal tax purposes in the current or later year consistent with the manner in which the item was treated in a pre-*Windsor* year for which an amended return is not being filed. For example, if a same-sex married couple is divorced in a Recognition State in a pre-*Windsor* year and one spouse issued an installment note to the other spouse as part of the property settlement with payments extending into a post-*Windsor* year, can the parties claim the tax-free benefits of Code Section 1041 in the post-*Windsor* year even though payments in the year of divorce were not reported under Code Section 1041. Conversely, as in the above corporate redemption example, if the redeeming shareholder received an installment note from the corporation with payments extending into a post-*Windsor* year, will the character of the gain on the redemption be taxed as capital gain in the post-*Windsor* year (which is consistent with the treatment in the original pre-*Windsor* redemption year) or taxed as ordinary income in the post-*Windsor* year since the redeeming spouse is now considered married to the

[23] The requirements for a claim for refund can be found at Treasury Regulations §§301.6402-2 and -3. The appropriateness and consequences of a protective claim for refund can be found at CCA 2011 36021 (9-9-11), GCM 38786 (8-13-81) and *Martin v. U.S.*, 833 F.2d 655 (7th Cir. 1987). A claim for refund that is determined to be for an excessive amount could trigger a penalty. Code Section 6676.
Treasury Regulation §20.2053-1(b)(5) addresses protective claims for refund in the estate tax area for uncertain deductions under Code Section 2053. *See also,* Rev. Proc. 2011-48, 2011-42 IRB 527.
[24] Code Sections 302 and 318.

remaining shareholder/spouse in the prior year who is a related party under Code Section 318 for purposes of Code Section 302(b)(3).

The duty of consistency requires a taxpayer to be consistent in the treatment of tax items under certain conditions.[25] How this duty applies in the situations described above is not clear since the potential inconsistency results not from the taxpayer's error or omission but from a change in a law that seemingly is retroactive.

In addition, it is not clear whether, in an IRS audit of one spouse to a same-sex marriage for a pre-*Windsor* year, the IRS can treat the taxpayer/spouse as married for federal tax purposes for the audit year even though the spouse filed as a single person.

2. Non-Recognition States. Until the Internal Revenue Service issues further guidance, it would appear at this time that same-sex married couples living during an applicable tax year in a Non-Recognition State will be required to file as unmarried persons for federal income tax purposes. However, since a possibility exists that the Internal Revenue Service or some other applicable authority may one day conclude that federal income tax laws will be applied on the basis of State of Ceremony, serious consideration must be given to whether a protective claim for refund should be filed for all open years (if a refund in tax would result from filing as married) in order to preserve the right to a refund and avoid the running of the statute of limitations for an otherwise open year at this time. The same logic would apply to years for which a federal income tax return is to be filed. For example, a same-sex married couple living in Texas during the tax year 2013 might want to consider filing a federal tax return for each spouse as single and then simultaneously file a protective claim for refund computing the combined tax on a married status basis for the same reasons as expressed above.

However, before a same-sex married couple living in a Non-Recognition State makes a final determination to file a protective claim for refund if such action is otherwise warranted, such couple should consider potential disadvantages from an income tax point of view from filing as married. Such disadvantages could arise in a number of areas, such as discussed above.

A same-sex married couple living in a Non-Recognition State seeking a divorce has a fundamental problem since such couple may not be able to obtain a divorce either in the Non-Recognition State or any other state in which the couple are not residents, including the State of Ceremony. For this couple, the property settlement will be a taxable event and the cash payments cannot qualify for alimony or child support under the Code. This couple does not have the alternative of filing an amended return since a divorce was never obtained.

[25] *Janis v. Commissioner*, 87 T.C.M. 1322 (2004).

B. Gift Tax.

1. Recognition States. For a same-sex married couple living in a Recognition State, the *Windsor* opinion affords this couple many gift tax advantages.

First, transfers of property between the spouses will be gift-tax free because the married couple will qualify for the unlimited marital deduction[26] and a gift tax return will not be required.

In addition, gifts of property to a third party will qualify for gift splitting, wherein the $14,000 annual exclusion per donee will be available from both the donor spouse and the non-donor spouse, thus qualifying the gift for a $28,000 annual gift tax exclusion per couple.[27] The same rationale applies to a spouse's lifetime exemption amount that currently is $5,250,000.[28]

If a transfer of property was made between spouses in a prior year for which a gift tax was paid, an amended gift tax return should be filed claiming the marital deduction and a refund of any gift taxes paid. If no gift taxes were paid with regard to a prior year's transfer of property for which a gift tax return was filed but the amount of the gift exceeded the annual exclusion and therefore utilized any portion the donor's lifetime exemption amount, an amended gift tax return should be filed claiming the marital deduction and thus reversing the use of the lifetime exclusion.

If a gift tax return was filed for a prior year and the applicable three (3) year / two (2) year statute of limitations has run, a question exists as to whether the filing of the amended gift tax return at this time would be effective. Since this uncertainty exists today, the better course of action will be to file an amended gift tax return claiming the marital deduction to at least correct, if ultimately permissible, the use of any of the lifetime exemption even if a refund of the actual gift tax paid might one day be denied because of the running of the applicable statute of limitations.

2. Non-Recognition States. For a same-sex married couple living in a Non-Recognition State, the same uncertainty that exists with regard to the income tax issues also exists with regard to the gift tax issues. If a transfer of property is contemplated between the spouses to a same-sex marriage, one course of action will be to treat the gift without regard to the marital deduction, file a gift tax return accordingly, pay whatever gift tax, if any, results and then file an amended gift tax return (or a protective claim for refund) claiming the marital deduction, a refund of any gift taxes paid, and a reduction in the amount of the lifetime exemption originally shown as used on the gift tax return.

[26] Code Section 2523.
[27] Code Section 2503(b).
[28] Code Sections 2505 and 2010(c).

With regard to prior years for which a gift tax return was filed, one course of action that should be considered is the filing of a protective claim for refund for the prior year claiming the marital deduction and a refund of any applicable gift tax paid and a reduction in the amount of the lifetime exemption originally shown as used. At a minimum, the filing of the protective claim for refund will stop the running of the statute of limitations, which would be beneficial if it takes several years for this uncertainty to be resolved. Otherwise, by the time the uncertainty is resolved and if resolved favorably towards a taxpayer, it may be too late to reap the benefit of the resolution of the issue if the statute of limitations for the applicable year has otherwise run.

For those years for which a gift tax return was filed and the applicable statute of limitations has run, consideration should be given as to whether a protective claim for refund should be filed for the reasons expressed above or not filed and defer action depending upon how this issue is ultimately resolved.

C. Estate Tax.

1. Recognition States. Same-sex married couples residing in Recognition States will be entitled to all the federal estate tax benefits accorded to opposite-sex married couples. These benefits include the unlimited marital deduction[29], which allows an estate tax deduction for the value of assets passing from the deceased spouse to the surviving spouse.

In addition, the recent addition to the Code of "portability," being an election made in the estate of the first deceased spouse, for the unused estate tax exemption of the first deceased spouse will be available to the same-sex surviving spouse.[30]

An issue relates to the portability election for the estate of the first deceased spouse.[31] IRS Notice 2011-82[32] requires the portability election for estates of decedents dying after 2010 be made on a timely filed federal estate tax return.[33] The due date of the estate return is nine (9) months after date of death plus a possible additional extension of six (6) months.[34] Obviously, by June 26, 2013, the time for making a portability election has expired for some previously filed (or unfiled) estate tax returns. Whether the IRS will grant additional time for the estate of a deceased spouse of a same-sex married couple to make the election remains to be seen.

In the case of an estate tax return previously filed for a deceased same-sex spouse in a Recognition State and who is survived by a same-sex spouse, consideration should

[29] Code Section 2056.
[30] Code Section 2010.
[31] Code Section 2010.
[32] 2011-42 IRB 516.
[33] *See also,* Treasury Regulations §20.2010-2T(a)(3).
[34] Code Sections 6075(a) and 6081(a).

be given to filing an amended estate tax return to utilize the unlimited marital deduction to the extent otherwise applicable (meaning estate assets pass to the surviving same-sex spouse) and to preserve for the surviving same-sex spouse the deceased same-sex spouse's unused estate tax exemption, if any. As in the gift tax area described above, the same issues and considerations need to be given to the applicability of the statute of limitations and filing an amended estate tax return.

2. Non-Recognition States. For a deceased same-sex spouse in a Non-Recognition State, it is not clear whether the unlimited marital deduction would be available. At the present, it appears that the answer is no. Nevertheless, if the unlimited marital deduction would be utilized if available, consideration should be given to filing an estate tax return without the unlimited marital deduction and then filing a protective claim for refund claiming the use of the unlimited marital deduction. Under current estate tax law, the unlimited marital deduction would be needed only to the extent the value of the assets passing to the surviving same-sex spouse exceeded the estate tax exemption of the first deceased spouse, which currently is $5,250,000.[35] In addition, such amended return should also claim the benefits of portability for any unused estate tax exemption in the estate of the first deceased same-sex spouse.

ESTATE PLANNING.

The dichotomy between Recognition States and Non-Recognition States will be the continual subject of future developments.

For now, planning and advice to same-sex couples requires diligence. Diligence includes both planning to obtain future benefits and advice as to claiming current federal benefits. Plans for same-sex couples should be reviewed and revised for the above-mentioned income, gift and estate tax benefits.

1. Recognition States. In Recognition States, estate plans should be immediately changed to take full advantage of marital deduction planning and split-gift planning.

In addition, plans should also be reviewed for couples as a result of this newly recognized marital status. For example, grantor retained income trusts (or "**GRITs**") have been a popular tool utilized for same-sex couples. This technique was available because as long as a same-sex partner was not considered to be a spouse, Chapter 14 of the Code was not applicable. GRITs are no longer available in Recognition States for same-sex married couples. In fact, prior year GRITs may be the subject of attack by the IRS. There are many such examples of planning matters which are altered due to the newly recognized marital status of some couples.

[35] Code Section 2010.

Another example is the status of existing trusts where a same-sex partner is serving as trustee. It is now possible that such a trust has been converted to a grantor trust under Subchapter J of the Code due to the grantor being deemed to have the powers of his or her newly-recognized spouse. The Code specifically addresses a change in marital status clarifying that one is deemed to hold the powers of a new spouse but only for periods following the establishment of the marital relationship.[36]

An additional question relating to the above type of trust involves the retroactive application of *Windsor*. Due to the *Windsor* opinion, could this trust be treated as a grantor trust since inception. This question remains unclear.

2. Non-Recognition States. Planning for same-sex couples in Non-Recognition States should focus on flexibility as it is possible, for federal tax purposes, that the status may some day be recognized. It is important that plans for same-sex couples be flexible enough to take advantage of the marital deduction if applicable at the death of one of the spouses. GRIT planning in a Non-Recognition State is still theoretically available for a same-sex married couple, but use of a GRIT in this case would appear at this time to be very risky.

3. State Law Issues. While not a direct result of the *Windsor* or *Perry* decisions, or, for that matter, DOMA, the continual and evolutionary acceptance of same-sex couples creates some significant state law implications for planning attorneys and other professionals. Specifically, any number of planning documents which address the concept of a "spouse" should, if not already, account for whether the term includes same-sex spouses or, if it is a general reference to spouse, then what law is intended to apply in determining whether one is a spouse for purposes of the document.

Further, references to "child" or "descendant" in a document should address what is meant by those terms and what law is to apply. A will or trust could itself define the beneficiaries of the Estate or Trust or define the class of appointees of a power of appointment.

In determining whether an individual is a beneficiary of a will or trust, a drafter could (1) attempt to carefully define the term in the document, (2) rely on modifying terms such as "legitimate," "blood," or "adopted," or (3) make reference to definition under applicable state law.

New estate documents should carefully consider how children of same-sex couples will be treated for purposes of the agreement. For example, assume a child is born with one parent in a same-sex couple being the biological parent. The document should address the question of whether the child is "legitimate" or whether the child is born in or out of wedlock if those terms are used in the document. The document should also answer the question of whether such child

[36] Code Section 672(e).

is a descendant of the non-biological parent. Care must be exercised in designating which state's laws are to be applied if any reliance is placed on state law for these determinations.

It is expected that *Windsor* will result in a dramatic increase in same-sex married couples due to the availability of federal economic benefits and, therefore, states will increasingly need to deal with the differing status applied to such couples and their descendants.

<u>CONCLUSION</u>.

While the Supreme Court in *Windsor* clarified the applicability of federal law to same-sex married couple in Recognition States, the Court did not address how those same couples are to be treated in Non-Recognition States. Hopefully, federal agencies, including the Internal Revenue Service, will quickly issue guidance in this area.

Frankly, we would hope that the federal agencies will apply federal law based on the State of Ceremony and not the State of Residency. Applying federal law on the basis of State of Ceremony will at least treat all similarly-situated same-sex married couples the same for federal purposes regardless of where they are living at any moment in time. Applying federal benefits on the basis of State of Residency not only treats similarly-situated couples differently but treats the same couple differently as that couple moves from state to state.

For example, a same-sex married couple in New York will be entitled to all the federal benefits during any given year in which they are residents in New York, including filing federal tax returns as married. However, if that same couple later moves to Texas, which is a Non-Recognition State, and if the federal tax laws were applied on the basis of State of Residency, then that same couple upon arriving in Texas would no longer be able to file federal tax returns as married but would have to file federal tax returns as single. In that case, a question would arise as to how certain tax benefits, such as net operating losses, that arose while the couple was a resident in New York and that were available to be used in subsequent years would be split between the couple after arriving in Texas.

In addition, a whole new set of rules would become applicable that were inconsistent with the rules that applied in the prior year. Trying to figure out the consequences of transitioning from a married return to a single return while the couple is still married would be time consuming and inexact.

Therefore, for the sake of simplicity and ease of administration, federal agencies should apply federal benefits on the basis of State of Ceremony. That application would not avoid conflict between the federal law and state law treatment but would at least apply federal law on a consistent basis from year to year regardless of which state the married couple resided.

Unfortunately, all federal agencies have not issued guidance as of the time of the writing of this article and, thus, the quagmire continues.

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